**COMMODITY FUTURES TRADING COMMISSION**

**17 CFR Parts 1, 15, 17, 19, 37, 38, 140, 150 and 151**

**RIN 3038–AD99**

# Position Limits for Derivatives

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Reproposal.

**SUMMARY:** The Commodity Futures Trading Commission (''Commission'' or ''CFTC'') is reproposing rules to amend part 150 of the Commission's regulations concerning speculative position limits to conform to the Wall Street Transparency and Accountability Act of 2010 (''Dodd-Frank Act'') amendments to the Commodity Exchange Act (''CEA'' or ''Act''). The reproposal would establish speculative position limits for 25 exempt and agricultural commodity futures and option contracts, and physical commodity swaps that are ''economically equivalent'' to such contracts (as such term is used in section 4a(a)(5) of the CEA). In connection with establishing these limits, the Commission is reproposing to update some relevant definitions; revise the exemptions from speculative position limits, including for bona fide hedging; and extend and update reporting requirements for persons claiming exemption from these limits. The Commission is also reproposing appendices to part 150 that would provide guidance on risk management exemptions for commodity derivative contracts in excluded commodities permitted under the revised definition of bona fide hedging position; list core referenced futures contracts and commodities that would be substantially the same as a commodity underlying a core referenced futures contract for purposes of the definition of location basis contract; describe and analyze fourteen fact patterns that would satisfy the reproposed definition of bona fide hedging position; and present the reproposed speculative position limit levels in tabular form. In addition, the Commission proposes to update certain of its rules, guidance and acceptable practices for compliance with Designated Contract Market (''DCM'') core principle 5 and Swap Execution Facility (''SEF'') core principle 6 in respect of exchange-set speculative position limits and position accountability levels. Furthermore, the Commission is reproposing processes for DCMs and SEFs to recognize certain positions in commodity derivative contracts as non-enumerated bona fide hedges or enumerated anticipatory bona fide hedges, as well as to exempt from position limits certain spread positions, in each case subject to Commission review. Separately, the Commission is reproposing to delay for DCMs and SEFs that lack access to sufficient swap position information the requirement to establish and monitor position limits on swaps.

**DATES:** Comments must be received on or before February 28, 2017.

**ADDRESSES:** You may submit comments, identified by RIN number 3038–AD99, by any of the following methods:

- *CFTC Web site: http://comments.cftc.gov*;
- *Mail:* Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street NW., Washington, DC 20581;
- *Hand delivery/courier:* Same as Mail, above.
- *Federal eRulemaking Portal: http://www.regulations.gov*. Follow instructions for submitting comments.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to *http://www.cftc.gov*. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that may be exempt from disclosure under the Freedom of Information Act, a petition for confidential treatment of the exempt information may be submitted according to the procedures established in CFTC regulations at 17 CFR part 145.

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

**FOR FURTHER INFORMATION CONTACT:** Stephen Sherrod, Senior Economist, (202) 418–5452, *ssherrod@cftc.gov*, Riva Spear Adriance, Senior Special Counsel, (202) 418–5494, *radriance@cftc.gov*, Hannah Ropp, Surveillance Analyst, 202–418–5228, *hropp@cftc.gov*, or Steven Benton, Industry Economist, (202) 418–5617, *sbenton@cftc.gov*, Division of Market Oversight; or Lee Ann Duffy, Assistant General Counsel, 202–418–6763, *lduffy@cftc.gov*, Office of General Counsel, in each case at the Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street NW., Washington, DC 20581.

**SUPPLEMENTARY INFORMATION:**

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## I. Background

### *A. Introduction*

The Commission has long established and enforced speculative position limits for futures and options contracts on various agricultural commodities as authorized by the Commodity Exchange

Act (''CEA'').[1] The part 150 position limits regime [2] generally includes three components: (1) The level of the limits, which set a threshold that restricts the number of speculative positions that a person may hold in the spot-month, individual month, and all months combined,[3] (2) exemptions for positions that constitute bona fide hedging transactions and certain other types of transactions,[4] and (3) rules to determine which accounts and positions a person must aggregate for the purpose of determining compliance with the position limit levels.[5]

In late 2013, the CFTC proposed to amend its part 150 regulations governing speculative position limits.[6] These proposed amendments were intended to conform the requirements of part 150 to particular changes to the CEA introduced by the Wall Street Transparency and Accountability Act of 2010 (''Dodd-Frank Act'').[7] The proposed amendments included the adoption of federal position limits for 28 exempt and agricultural commodity futures and option contracts and swaps that are ''economically equivalent'' to such contracts.[8] In addition, the Commission proposed to require that DCMs and SEFs that are trading facilities (collectively, ''exchanges'') establish exchange-set limits on such futures, options and swaps contracts.[9] Further, the Commission proposed to (i) revise the definition of bona fide hedging position (which includes a general definition with requirements applicable to all hedges, as well as an enumerated list of bona fide hedges),[10] (ii) revise the process for market participants to request recognition of certain types of positions as bona fide hedges, including anticipatory hedges and hedges not specifically enumerated in the proposed bona fide hedging definition; [11] and (iii) revise the exemptions from position limits for transactions normally known to the trade as spreads.[12]

On June 13, 2016, the Commission published a supplemental proposal to its December 2013 Position Limits rulemaking.[13] The supplemental proposal included revisions and additions to regulations and guidance proposed in 2013 concerning speculative position limits in response to comments received on that proposal, and alternative processes for DCMs and SEFs to recognize certain positions in commodity derivative contracts as non-enumerated bona fide hedges or enumerated anticipatory bona fide hedges, as well as to exempt from federal position limits certain spread positions, in each case subject to Commission review. In this regard, under the 2016 Supplemental Position Limits Proposal, certain of the regulations proposed in 2013 regarding exemptions from federal position limits and exchange-set position limits would be amended to take into account the alternative processes. In connection with those proposed changes, the Commission proposed to further amend certain relevant definitions, including to clearly define the general definition of bona fide hedging for physical commodities under the standards in CEA section 4a(c). Separately, the Commission proposed to delay for DCMs and SEFs that lack access to sufficient swap position information the requirement to establish and monitor position limits on swaps at this time.

After review of the comments responding to both the December 2013 Position Limits Proposal and the 2016 Supplemental Position Limits Proposal, the Commission, in consideration of those comments, is now issuing a reproposal (''Reproposal''). The Commission invites comments on all aspects of this Reproposal.

### *B. The Commission Preliminarily Construes CEA Section 4a(a) To Mandate That the Commission Impose Position Limits*

#### 1. Introduction

#### a. The History of Position Limits and the 2011 Position Limits Rule

As part of the Dodd-Frank Act, Congress amended the CEA's position limits provision, which since 1936 has authorized the Commission (and its predecessor) to impose limits on speculative positions to prevent the harms caused by excessive speculation. Prior to the Dodd-Frank Act, CEA section 4a(a) stated that for the purpose of diminishing, eliminating or preventing specified burdens on interstate commerce, the Commission shall, from time to time, after due notice and an opportunity for hearing, by rule, regulation, or order, proclaim and fix such limits on the amounts of trading which may be done or positions which may be held by any person under contracts of sale of such commodity for future delivery on or subject to the rules of any contract market as the Commission finds are necessary to

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[1] 7 U.S.C. 1 *et seq.*

[2] *See* 17 CFR part 150. Part 150 of the Commission's regulations establishes federal position limits (that is, position limits established by the Commission, as opposed to exchange-set limits) on certain enumerated agricultural contracts; the listed commodities are referred to as enumerated agricultural commodities. The position limits on these agricultural contracts are referred to as ''legacy'' limits because these contracts on agricultural commodities have been subject to federal position limits for decades. *See also* Position Limits for Derivatives, 78 FR 75680 at 75723, n. 370 and accompanying text (Dec. 12, 2013) (''December 2013 Position Limits Proposal'').

[3] *See* 17 CFR 150.2.

[4] *See* 17 CFR 150.3.

[5] *See* 17 CFR 150.4.

[6] *See generally* December 2013 Positions Limits Proposal. In the December 2013 Position Limits Proposal, the Commission proposed to amend its position limits to also encompass 28 exempt and agricultural commodity futures and options contracts and the physical commodity swaps that are economically equivalent to such contracts.

[7] The Commission previously had issued proposed and final rules in 2011 to implement the provisions of the Dodd-Frank Act regarding position limits and the bona fide hedge definition. Position Limits for Derivatives, 76 FR 4752 (Jan. 26, 2011); Position Limits for Futures and Swaps, 76 FR 71626 (Nov. 18, 2011). A September 28, 2012 order of the U.S. District Court for the District of Columbia vacated the November 18, 2011 rule, with the exception of the rule's amendments to 17 CFR 150.2. *International Swaps and Derivatives Association* v. *United States Commodity Futures Trading Commission,* 887 F. Supp. 2d 259 (D.D.C. 2012). *See generally* the materials and links on the Commission's Web site at *http://www.cftc.gov/LawRegulation/DoddFrankAct/Rulemakings/DF_26_PosLimits/index.htm.* The Commission issued the December 2013 Position Limits Proposal, among other reasons, to respond to the District Court's decision in *ISDA* v. *CFTC. See generally* the materials and links on the Commission's Web site at *http://www.cftc.gov/LawRegulation/DoddFrankAct/Rulemakings/PositionLimitsforDerivatives/index.htm.*

[8] *See* CEA section 4a(a)(5), 7 U.S.C. 6a(a)(5) (providing that the Commission establish limits on economically equivalent contracts); CEA section 4a(a)(6), 7 U.S.C. 6a(a)(6) (directing the Commission to establish aggregate position limits on futures, options, economically equivalent swaps, and certain foreign board of trade contracts in agricultural and exempt commodities (collectively, ''referenced contracts'')). *See* December 2013 Position Limits Proposal, 78 FR at 75825. Under the December 2013 Position Limits Proposal, ''referenced contracts'' would have been defined as futures, options, economically equivalent swaps, and certain foreign board of trade contracts, in physical commodities, and been subject to the proposed federal position limits. The Commission proposed that federal position limits would apply to referenced contracts, whether futures or swaps, regardless of where the futures or swaps positions were established. *See* December 2013 Positions Limits Proposal, at 78 FR 75826 (proposed § 150.2).

[9] *See* December 2013 Position Limits Proposal, 78 FR at 75754–8. Consistent with DCM Core Principle 5 and SEF Core Principle 6, the Commission proposed at § 150.5(a)(1) that for any commodity derivative contract that is subject to a speculative position limit under § 150.2, a DCM or SEF that is a trading facility shall set a speculative position limit no higher than the level specified in § 150.2.

[10] *See* December 2013 Position Limits Proposal, 78 FR at 75706–11, 75713–18.

[11] *See* December 2013 Position Limits Proposal, 78 FR at 75718.

[12] *See* December 2013 Position Limits Proposal, 78 FR at 75735–6. CEA section 4a(a)(1), 7 U.S.C. 6a(a)(1), permits the Commission to exempt transactions normally known to the trade as ''spreads'' from federal position limits.

[13] Position Limits for Derivatives: Certain Exemptions and Guidance, 81 FR 38458 (June 13, 2016) (''2016 Supplemental Position Limits Proposal'').

diminish, eliminate, or prevent such burden.[14]

In the Dodd-Frank Act, Congress renumbered a modified version of CEA section 4a(a) as section 4a(a)(1) and added, among other provisions, CEA section 4a(a)(2), captioned ''Establishment of Limitations,'' which provides that in accordance with the standards set forth in CEA section 4a(a)(1), the Commission shall establish limits on the amount of positions, as appropriate, other than bona fide hedge positions, that may be held by any person. CEA section 4a(a)(2) further provides that for exempt commodities (energy and metals), the limits required under CEA section 4a(a)(2) shall be established within 180 days after the date of the enactment of CEA section 4a(a)(2); for agricultural commodities, the limits required under CEA section 4a(a)(2) shall be established within 270 days after the date of the enactment of CEA section 4a(a)(2).[15]

These and other changes to CEA section 4a(a) are described in more detail below.

Pursuant to these amendments, the Commission adopted a position limits rule in 2011 (''2011 Position Limits Rule'') in a new part 151.[16] In the 2011 Position Limits Rule, the Commission imposed, in new part 151, speculative limits in the spot-month and non-spot-months on 28 physical commodity derivatives ''of particular significance to interstate commerce.'' [17] Under the 2011 Position Limits Rule, part 151 used formulas for calculating limit levels that are similar to the formulas used to calculate previous Commission- and exchange-set position limits.[18] The 2011 Position Limits Rule contained provisions in part 151 that implemented the statutory exemption for bona fide hedging.[19] It also provided account aggregation standards to determine which positions to attribute to a particular market participant.[20] Because it interpreted the Dodd-Frank Act as mandating position limits, the Commission did not make an independent threshold determination that position limits are necessary to accomplish the purposes set forth in the statute. The Commission explained:

> Congress directed the Commission to impose position limits and to do so expeditiously. Section 4a(a)(2)(B) states that the limits for physical commodity futures and options contracts ''shall'' be established within the specified timeframes, and section 4a(a)(2)(5) states that the limits for economically equivalent swaps ''shall'' be established concurrently with the limits required by section 4a(a)(2). The congressional directive that the Commission set position limits is further reflected in the repeated references to the limits ''required'' under section 4a(a)(2)(A).[21]

ISDA and SIFMA sued the Commission to vacate part 151 on the basis (among others) that, in their view, CEA section 4a(a) clearly required the Commission to make an antecedent necessity finding.

b. The District Court Opinion

As set forth in the Commission's December 2013 Position Limits Proposal,[22] the district court in *ISDA* v. *CFTC* found that, on one hand, CEA section 4a(a)(1) ''unambiguously requires that, prior to imposing position limits, the Commission find that position limits are necessary to 'diminish, eliminate, or prevent' the burden described in [CEA section 4a(a)(1)].'' [23] On the other hand, the court found that the Dodd-Frank Act amendments to CEA section 4a(a) rendered section 4a(a)(1) ambiguous with respect to whether such findings are required for the position limits described in CEA section 4a(a)(2)—futures contracts, options, and certain swaps on agricultural and exempt commodities.[24]

The court's determination in *ISDA* v. *CFTC* that CEA sections 4a(a)(1) and (2), read together, are ambiguous focused on the opening phrase of subsection (A)—''[i]n accordance with the standards set forth in [CEA section 4a(a)(1)].'' The court held that the term ''standards'' in CEA section 4a(a)(2) was ambiguous as to whether it referred to the requirement in CEA section 4a(a)(1) that the Commission impose position limits only ''as [it] finds are necessary to diminish, eliminate, or prevent'' an unnecessary burden on interstate commerce.[25] If not, ''standards'' would refer to the aggregation and flexibility standards stated in CEA section 4a(a)(1) by which position limits are to be implemented. Accordingly, the court rejected both (1) the Commission's contention that CEA section 4a(a) as a whole unambiguously mandated the imposition of position limits without the Commission finding independently that they are necessary; and (2) the plaintiffs' contention that CEA section 4a(a) unambiguously required the Commission to make such findings before the imposition of position limits.[26] The court stated that because the Commission had incorrectly found CEA section 4a(a) unambiguous, it could not defer to any interpretation by the Commission to resolve the section's ambiguity. As the court observed, the D.C. Circuit has held that '' 'deference to an agency's interpretation of a statute is not appropriate when the agency wrongly believes that interpretation is compelled by Congress.' '' [27] The court further held that, pursuant to the law of the D.C. Circuit, it was required to remand the matter to the Commission so that it could ''fill in the gaps and resolve the ambiguities.'' [28] The court instructed that the Commission must apply its experience and expertise and cautioned that, in resolving the ambiguity in CEA section 4a(a), '' 'it is incumbent upon the agency not to rest simply on its parsing of the statutory language.' '' [29] The Commission does not rest simply on parsing the statutory language, but any interpretation necessarily begins with the text, which is described in the next section.

2. The Statutory Framework for Position Limits

Before the Dodd-Frank Act, what was then CEA section 4a(a) authorized the

[14] 7 U.S.C. 6a(a) (2006).

[15] CEA section 4a(a)(2); 7 U.S.C. 6a(a)(2). The Commission notes that it uses the defined term ''bona fide hedging position'' throughout part 150, rather than ''bona fide hedge positions'' found in CEA section 4a(a)(2). CEA section 4a(c)(1) uses the term ''bona fide hedging transactions or positions'' and CEA section 4a(c)(2) uses the term ''bona fide hedging transaction or position.'' The Commission interprets all of these terms to mean the same. It should be noted that the Commission previously imposed transaction volume limits on ''the amounts of trading which may be done'' as authorized by CEA section 4a(a)(1), but removed those transaction volume limits. Elimination of Daily Speculative Trading Limits, 44 FR 7124, 7127 (Feb. 6, 1979).

[16] Position Limits for Futures and Swaps, 76 FR 71626 (Nov. 18, 2011). As finalized, part 151 replaced part 150.

[17] *Id.* at 71665; *see also id* at 716629–30.

[18] *Id.* at 71632–33 (transition), 71668–70 (spot-month limit), 71671 (non-spot month limit).

[19] *Id.* at 71643–51.

[20] *Id.* at 71651–55. A central feature of any position limits regime is determining which positions to attribute to a particular trader. The CEA requires the Commission to attribute to a person all positions that the person holds or trades, as well as positions held or traded by anyone else that such person directly or indirectly controls. 7 U.S.C. 6a(a)(1). This is referred to as account aggregation. In addition to account aggregation, Congress required the Commission to set limits on all derivative positions in the same underlying commodity that a trader may hold or control across all derivative exchanges. 7 U.S.C. 6a(a)(6). The Commission refers to this as position aggregation.

[21] Position Limits for Futures and Swaps, 76 FR at 71626–628.

[22] *International Swaps and Derivatives Ass'n* v. *United States Commodity Futures Trading Comm'n,* 887 F. Supp. 2d 259 (D.D.C. 2012).

[23] *Id.* at 270.

[24] *Id.* at 281.

[25] 887 F. Supp. 2d at 274–76.

[26] 887 F. Supp. 2d at 279–80.

[27] *Id.* at 280–82, quoting *Peter Pan Bus Lines, Inc.* v. *Fed. Motor Carrier Safety Admin.,* 471 F.3d 1350, 1354 (D.C. Cir. 2006).

[28] 887 F. Supp. 2d at 282.

[29] *Id.* at n.7, quoting *PDK Labs. Inc.* v. *DEA,* 362 F.3d 786, 797 (D.C. Cir. 2004).

Commission to set limits on futures for any exchange-traded contract for future delivery of any commodity ''as the Commission finds are necessary to diminish, eliminate, or prevent [the] burden'' of ''[e]xcessive speculation'' ''causing sudden or unreasonable fluctuations or unwarranted changes in the price of such commodity.'' 7 U.S.C. 6a(a) (2009 Supp.).[30] CEA section 4a(a) also required the Commission to follow certain criteria for aggregating limits once it made that determination. And the Commission was authorized to impose limits flexibly, depending on the commodity, delivery month, and other factors.[31]

The 2010 Dodd-Frank Act amendments to CEA section 4a(a) significantly expanded and altered it. The entirety of pre-Dodd-Frank CEA section 4a(a) became CEA section 4a(a)(1). Congress added six new subsections to CEA section 4a(a)—sections 4a(a)(2) through (7). And, outside of section 4a(a), Congress imposed a requirement that the Commission study the new limits it imposed and provide Congress with a report on their effects within one year of their imposition.[32]

The primary change at issue here was the addition of new CEA section 4a(a)(2), which addresses position limits on a specific class of commodity contracts, ''physical commodities other than excluded commodities'':

CEA section 4a(a)(2)(A) provides that in accordance with the standards set forth in CEA section 4a(a)(1), with respect to physical commodities other than excluded commodities, the Commission shall establish limits on the amount of positions, as appropriate, other than bona fide hedge positions, that may be held by any person with respect to contracts of sale for future delivery or with respect to options on the contracts.

CEA section 4a(a)(2)(B), in turn, provides that the limits ''required'' under CEA section 4a(a)(2)(A) ''shall be established within 180 days after the date of enactment of this paragraph'' for ''agricultural commodities'' (such as wheat or corn) and ''within 270 days after the date of the enactment of this paragraph'' for ''exempt commodities'' (which include energy-related commodities like oil, as well as metals).[33]

The other new subsections of CEA section 4a(a) delineate the types of physical commodity derivatives to which the new limits apply, set forth criteria for the Commission to consider in determining the levels of the required limits, require the Commission to aggregate the limits across exchanges for equivalent derivatives, require the Commission to impose limits on swaps that are economically equivalent to the physical commodity futures and options subject to CEA section 4a(a)(2), and permit the Commission to grant exemptions from the position limits it must impose under the provision:

- Section 4a(a)(3) guides the Commission in setting appropriate limit levels by providing that the Commission shall consider whether the limit levels: (i) Diminish, eliminate, or prevent excessive speculation; (ii) deter and prevent market manipulation, squeezes, and corners; (iii) ensure sufficient market liquidity for bona fide hedgers; and (iv) ensure that the price discovery function of the underlying market is not disrupted;
- Section 4a(a)(4) sets forth criteria for determining which swaps perform a significant price discovery function for purposes of the position limits provisions;
- Section 4a(a)(5) requires the Commission to concurrently impose appropriate limit levels on physical commodity swaps that are economically equivalent to the futures and options for which limits are required;
- Section 4a(a)(6) requires the Commission to apply the required position limits on an aggregate basis to contracts based on the same underlying commodity across all exchanges; and
- Section a(a)(7) authorizes the Commission to grant exemptions from the position limits it imposes.[34]

In a separate Dodd-Frank Act provision, Congress required that the Commission, in consultation with exchanges, ''shall conduct a study of the effects (if any) of the position limits imposed'' under CEA section 4a(a)(2), that ''[w]ithin twelve months after the imposition of position limits'' the Commission ''shall'' submit a report of the results of the study to Congress, and that Congress ''shall'' hold hearings within 30 days of receipt of the report regarding its findings.[35]

3. The Commission's Experience With Position Limits

As explained in the December 2013 Position Limits Proposal, position limits have a long history as a tool to prevent unwarranted price movement and volatility, including but not limited to price swings caused by market manipulation.[36] Physical commodities underlying futures contracts are, by definition, in finite supply, and so it is

[30] Under the heading of ''Burden on interstate commerce; trading or position limits,'' 7 U.S.C. 6a(a) (2006) provided that excessive speculation in any commodity under contracts of sale of such commodity for future delivery made on or subject to the rules of contract markets or derivatives transaction execution facilities, or on electronic trading facilities with respect to a significant price discovery contract causing sudden or unreasonable fluctuations or unwarranted changes in the price of such commodity, is an undue and unnecessary burden on interstate commerce in such commodity. Title 7 U.S.C. 6a(a) (2006) further provided that for the purpose of diminishing, eliminating, or preventing such burden, the Commission shall, from time to time, after due notice and opportunity for hearing, by rule, regulation, or order, proclaim and fix such limits on the amounts of trading which may be done or positions which may be held by any person under contracts of sale of such commodity for future delivery on or subject to the rules of any contract market or derivatives transaction execution facility, or on an electronic trading facility with respect to a significant price discovery contract, as the Commission finds are necessary to diminish, eliminate, or prevent such burden. Additionally, 7 U.S.C. 6a(a) (2006) stated that in determining whether any person has exceeded such limits, the positions held and trading done by any persons directly or indirectly controlled by such person shall be included with the positions held and trading done by such person; and further, such limits upon positions and trading shall apply to positions held by, and trading done by, two or more persons acting pursuant to an expressed or implied agreement or understanding, the same as if the positions were held by, or the trading were done by, a single person. Title 7 U.S.C. 6a(a) (2006) further stated that nothing in that section shall be construed to prohibit the Commission from fixing different trading or position limits for different commodities, markets, futures, or delivery months, or for different number of days remaining until the last day of trading in a contract, or different trading limits for buying and selling operations, or different limits for the purposes of paragraphs (1) and (2) of subsection (b) of this section, or from exempting transactions normally known to the trade as ''spreads'' or ''straddles'' or ''arbitrage'' or from fixing limits applying to such transactions or positions different from limits fixed for other transactions or positions. Moreover, 7 U.S.C. 6a(a) (2006) defined the word ''arbitrage'' in domestic markets to mean the same as a ''spread'' or ''straddle.'' It also authorized the Commission to define the term ''international arbitrage.'' 7 U.S.C. 6a(a) (2006).

[31] There were four other subsections of CEA section 4a: CEA section 4a(b), which made it unlawful for a person to hold positions in excess of Commission-set limits; CEA section 4a(c), which exempted positions held under an exemption for bona fide hedges, CEA section 4a(d), which exempted positions held by or on behalf of the United States, and CEA section 4a(e), which authorized exchanges to set limits so long as they were not higher than Commission-set limits and made it unlawful for any person to hold limits in excess of exchange-set limits. (Exchange-set limits are also addressed elsewhere in the CEA. *E.g.,* 7 U.S.C. 7(d)(5)).

[32] 15 U.S.C. 8307(a). Some parts of pre Dodd-Frank CEA sections 4a(a) and 4a(b)–(e) were also amended by the Dodd-Frank Act. CEA section 4a(a) is now CEA section 4a(a)(1) and was modified primarily to add swaps, CEA section 4a(b) updates the names of applicable exchanges, and CEA section 4a(c) requires the Commission to promulgate a rule in accordance with a narrowed definition of bona fide hedging position as an exemption from position limits. 7 U.S.C. 6a(a)(1), 6a(b)–(e).

[33] 7 U.S.C. 6a(a)(2)(B)(i) and (ii).

[34] 7 U.S.C. 6a(a)(3)–(7).

[35] 15 U.S.C. 8307(a).

[36] December 2013 Position Limits Proposal, 78 FR at 75685.

possible to amass or dissipate an extremely large position in such a way as to interfere with the normal forces of supply and demand. Speculators (who have no commercial use for the underlying commodity) are considered differently from hedgers (who use commodity derivatives to hedge commercial risk). Speculators have been considered a greater source of risk because their trading is unconnected with underlying commercial activity, whereas a hedger's trading is calibrated to other business needs. In various statutory enactments, Congress has recognized both the utility of position limits and the need to treat speculators differently from hedgers.

Congress began regulating commodity derivatives in 1917, when Congress enacted emergency legislation to stabilize the U.S. grain markets during the First World War by suspending wheat futures and securing ''a voluntary limitation'' of 500,000 bushels on trading in corn futures.[37] In 1922 Congress enacted the Grain Futures Act, in which it noted that ''sudden or unreasonable fluctuations in the prices of commodity futures . . . frequently occur as a result of speculation, manipulation, or control . . . .'' [38] In 1936, Congress strengthened the government's authority by providing for limits on speculative trading in commodity derivatives when it enacted the CEA. The CEA authorized the CFTC's predecessor, the Commodity Exchange Commission (CEC), to establish limits on speculative trading. Since that time, the Commission has been establishing or authorizing position limits for the past 80 years. As discussed in the December 2013 Position Limits Proposal and prior rulemakings, this history includes setting position limits beginning in 1938; overseeing exchange-set limits beginning in the 1960s; promulgating a rule in 1981, later directly ratified by Congress, mandating that exchanges set limits for all commodity futures for which there were no limits; allowing exchanges, in the 1990s, to set position accountability levels for certain financial contracts, such as futures and options on foreign currencies and other financial instruments with high degrees of stability; [39] and later expanding exchange limits or accountability requirements to significant price discovery contracts traded on exempt commercial markets.[40]

As addressed in the December 2013 Position Limits Proposal, two aspects of the Commission's experience are particularly important to the Commission's interpretation of the Dodd-Frank Act amendments to CEA section 4a. The first is the Commission's experience with the time required to make necessity findings before setting limits, which relates to the time limits contained in CEA section 4a(a)(2)(B). The second is the Commission's experience in rulemaking requiring exchanges to set limits in accordance with certain ''standards,'' the term the district court found ambiguous.

a. Time to Establish Position Limits

Based on its experience administering position limits, the Commission preliminarily concludes (as stated preliminarily in the December 2013 Position Limits Proposal) that Congress could not have contemplated that, as a prerequisite to imposing limits, the Commission would first make antecedent commodity-by-commodity necessity determinations in the 180–270 day time frame within which CEA section 4a(a)(2)(B) states that limits ''required under subparagraph [4a(a)(2(A)] shall be established.'' [41] As described in the December 2013 Position Limits Proposal, for 45 years after passage of the CEA, the Commission's predecessor agency made findings of necessity in its rulemakings establishing position limits.[42] During that period, the Commission had jurisdiction over only a limited number of agricultural commodities. In orders issued by the Commodity Exchange Commission between 1940 and 1956 establishing position limits, the CEC stated that the limits it was imposing in each were necessary. Each of those orders involved no more than a small number of commodities. But it took the CEC many months to make those findings. For example, in 1938, the CEC imposed position limits on six grain products.[43] Proceedings leading up to the establishment of the limits commenced more than 13 months earlier, when the CEC issued a notice of hearing regarding the limits.[44] Similarly, in September 1939, the CEC issued a Notice of Hearing with respect to position limits for cotton, but it was not until August 1940 that the CEC finally promulgated such limits.[45] And the CEC began the process of imposing limits on soybeans and eggs in January 1951, but did not complete the process until more than seven months later.[46]

In the Commission's experience (including the experience of its predecessor agency), it generally took many months to make a necessity finding with respect to one commodity. The process of making the sort of necessity findings that plaintiffs in *ISDA* v. *SIFMA* urged with respect to all agricultural commodities and all exempt commodities (and that some commenters urge) would be far more lengthy than the time allowed by CEA section 4a(a)(3), *i.e.,* 180 or 270 days from enactment of the Dodd-Frank Act.[47] Because of the stringent time limits in CEA section 4a(a)(2)(B), the Commission concludes that Congress did not intend for the Commission to delay the imposition of limits until it first made antecedent, contract-by-contract necessity findings.

[37] Frank M. Surface, *The Grain Trade During the World War,* at 224 (Macmilliam 1928).

[38] Grain Futures Act of 1922, ch. 369 at section 3, 342 Stat. 998, 999 (1922), codified at 7 U.S.C. 5 (1925–26).

[39] *See* Speculative Position Limits—Exemptions From Commission Rule 1.61; Chicago Mercantile Exchange Proposed Amendments to Rules 3902.D, 5001.E, 3010.F, 3012.F, 3013.F, 3015.F, 4604, and Deletion of Rules 3902.F, 5001.G, 3010.H., 3012.M, 3013.H, and 3015.H, 56 FR 51687 (Oct. 15, 1991) (providing notice of proposed exchange rule changes; request for comments). The Government, either through Congress, CEC or the Commission, has maintained position limits on various agricultural commodities since 1917.

[40] December 2013 Position Limits Proposal, 78 FR at 75681–85; Significant Price Discovery Contracts on Exempt Commercial Markets, 74 FR 12178 (March 23, 2009).

[41] December 2013 Position Limits Proposal, 78 FR at 75682–83 (citing 887 F. Supp. 2d at 273).

[42] *887 F. Supp. 2d* at 269.

[43] *See* In the Matter of Limits on Position and Daily Trading in Wheat, Corn, Oats, Barley, Rye, and Flaxseed, for Future Delivery Findings of Fact, Conclusions, and Order, 3 FR 3145, Dec. 24, 1938.

[44] *See* 2 FR 2460, Nov. 12, 1937.

[45] *See* Limitation on Buying or Selling of Cotton Notice of Hearing, 4 FR 3903, Sep. 14, 1939; Part 150—Orders of the Commodity Exchange Commission Findings of Fact, Conclusions, and Order In the Matter of Limits on Position and Daily Trading in Cotton for Future Delivery, 5 FR 3198, Aug. 28, 1940.

[46] *See* Handling of Anti-Hog-Cholera Serum and Hog-Cholera Virus; Notice of Proposed Rule Making 16 FR 321, Jan. 12, 1951; Limits on Position and Daily Trading in Eggs for Future Delivery, 16 FR 8106, Aug. 16, 1951; *see also* Limits on Positions and Daily Trading in Cottonseed Oil, Soybean Oil, and Lard for Future Delivery, 17 FR 6055, Jul. 4, 1952 (providing notice of a hearing regarding proposed position limits for cottonseed oil, soybean oil, and lard); Limits on Position and Daily Trading in Cottonseed Oil for Future Delivery, 18 FR 443, Jan. 22, 1953 (giving orders setting limits for cottonseed oil, soybean oil, and lard); Limits on Position and Daily Trading in Onions for Future Delivery; Notice of Hearing, 21 FR 1838, Mar. 24, 1956 (conveying notice of a hearing regarding proposed position limits for onions), Limits on Position and Daily Trading in Onions for Future Delivery, 21 FR 5575, Jul. 25, 1956 (providing order setting position limits for onions).

[47] Although the Commission did not meet these deadlines in its first position limits rulemaking, it completed the task (in which the Commission received and addressed more than 15,000 comments) as expeditiously as possible under the circumstances.

b. Prior Rulemaking Requiring Exchanges to Set Limits

The CFTC's preliminary interpretation of the statute is also based in part on its promulgation of a rule in 1981 requiring exchanges to impose limits on all contracts that did not already have limits. In that rulemaking, the Commission, acting expressly pursuant to, *inter alia,* what was then CEA section 4a(1) (predecessor to CEA section 4a(a)(1)), adopted what was then 17 CFR 1.61.[48] This rule required exchanges to set speculative position limits ''for each separate type of contract for which delivery months are listed to trade'' on any DCM, including ''contracts for future delivery of any commodity subject to the rules of such contract market.'' [49] The Commission explained that this action would ''close the existing regulatory gap whereby some but not all contract markets [we]re subject to a specified speculative position limit.'' [50]

Like the Dodd-Frank Act, the 1981 final rule established (and the rule release described) that such limits ''shall'' be established according to what the Commission termed ''standards.'' [51] As used in the 1981 final rule and release, ''standards'' meant the criteria for determining how the required limits would be set.[52] ''Standards'' did not include the antecedent ''necessity'' determination of *whether* to order limits at all. The Commission had already made the antecedent judgment in the rule that ''speculative limits are appropriate for all contract markets irrespective of the characteristics of the underlying market.'' [53] The Commission further concluded that, with respect to any particular market, the ''existence of historical trading data'' showing excessive speculation or other burdens on that market is not ''an essential prerequisite to the establishment of a speculative limit.'' [54]

The Commission thus directed the exchanges to set limits for all futures contracts ''pursuant to the . . . standards of rule 1.61,'' without requiring that the exchanges first make a finding of necessity.[55] And rule 1.61 incorporated the ''standards'' from then-CEA-section 4a(1)—an ''Aggregation Standard'' (46 FR at 50943) for applying the limits to positions both held and controlled by a trader, and a flexibility standard allowing the exchanges to set ''different and separate position limits for different types of futures contracts, or for different delivery months, or from exempting positions which are normally known in the trade as 'spreads, straddles or arbitrage' or from fixing limits which apply to such positions which are different from limits fixed for other positions.'' [56] Because the Commission had already made the antecedent necessity findings, it imposed tight deadlines for the exchanges to establish the limits. It is, accordingly, reasonable to believe that Congress would have structured CEA section 4a(a) similarly, by first making the antecedent necessity determination on its own,[57] then directing the Commission to impose the limits without making an independent determination of necessity, and then using the term ''standards'' just as the Commission did in 1981 to refer to aggregation and flexibility rather than necessity for the required limits.

Indeed, legislative history shows reason to believe that Congress' choice of the word ''standards'' to refer to aggregation and flexibility alone was purposeful and intended it to mean the same thing it did in the Commission's 1981 rule.[58] The language that ultimately became section 737 of the Dodd-Frank Act, amending CEA section 4a(a), originated in substantially final form in H.R. 977, introduced by Representative Peterson, who was then Chairman of the House Agriculture Committee and who would ultimately be a member of the Dodd-Frank Act conference committee.[59] In important respects, the language of H.R. 977 resembles the language the Commission used in 1981, suggesting that the regulation's text may have influenced the statutory text. Like the Commission's 1981 rule, H.R. 977 states that there ''shall'' be position limits in accordance with the ''standards'' identified in CEA section 4a(a).[60] This language was included in CEA section 4a(a)(2) as adopted. Also like the 1981 rule, H.R. 977 established (and the Dodd-Frank Act ultimately adopted) a ''good faith'' exception for positions acquired prior to the effective date of the mandated limits.[61] The committee report accompanying H.R. 977 described it as ''Mandat[ing] the CFTC to set speculative position limits'' and the section-by-section analysis stated that the legislation ''requires the CFTC to set appropriate position limits for all physical commodities other than excluded commodities.'' [62] This closely resembles the omnibus prophylactic approach the Commission took in 1981, when the Commission required the establishment of position limits on all futures contracts according to ''standards'' it borrowed from CEA section 4a(1). The Commission views the history and interplay of the 1981 rule and Dodd-Frank Act section 737 as further evidence that Congress intended to follow much the same approach as the Commission did in 1981, mandating position limits as to all physical commodities.[63]

There is further evidence based on the 1981 rulemaking that Congress would have found the across-the-board prophylactic approach attractive. In 1983, when enacting the Futures Trading Act of 19982, Public Law 97–444, 96 Stat. 2294 (1983), Congress was aware that the Commission had ''promulgated a final rule requiring exchanges to submit speculative position limit proposals for Commission approval for all futures contracts traded as of that date.'' [64] Presented with competing industry and Commission proposals to amend the position limits statute, Congress elected to amend the

[48] Establishment of Speculative Position Limits, 46 FR 50938, 50944–45, Oct. 16, 1981. The rule adopted in 1981 tracked, in significant part, the language of CEA section 4a(1). *Compare* 17 CFR 1.61(a)(1) (1982) *with* 7 U.S.C. 6a(1) (1976).

[49] Establishment of Speculative Position Limits, 46 FR at 50945.

[50] *Id.* at 50939; *see also id.* at 50938 (''to ensure that each futures and options contract traded on a designated contract market will be subject to speculative position limits'').

[51] *Compare id.* at 50941–42, 50945 *with* 7 U.S.C. 6a(a)(2)(A).

[52] Establishment of Speculative Position Limits, 46 FR 50941–42, 50945.

[53] *Id.* at 50941–42 (preamble), 50945 (text of § 1.61(a)(2)).

[54] The Commission believes it likely that, given the prophylactic purposes articulated in current CEA section 4a(a)(1)(A), a similar view of position limits underpins CEA section 4a(a)(2)(A).

[55] *Establishment of Speculative Position Limits.* 46 FR at 50942.

[56] *Id.* at 50945 (§ 1.61(a)). *Compare* 7 U.S.C. 6a(1) (1976).

[57] As discussed in further detail regarding congressional investigations, below, it is especially reasonable to infer that Congress had in fact made such a determination based on the congressional investigations that preceded these Dodd-Frank Act amendments. The fact that the Commission already had the clear authority to impose limits when *it* deemed them necessary bolsters this inference, because there was no need for these Dodd-Frank Act amendments to the position limits statute unless Congress, based on its own determination of necessity, sought to direct the Commission to impose limits.

[58] The relevant broader legislative history is discussed in depth, below.

[59] H.R. 977, 11th Cong. (2009).

[60] 7 U.S.C. 6.

[61] *Compare* H.R. 977, 11th Cong. (2009) *with* Establishment of Speculative Position Limits, 46 FR at 50944.

[62] H.Rept. 111–385, at 15, 19 (Dec. 19, 2009).

[63] *See Union Carbide Corp. & Subsidiaries* v. *Comm'r of Internal Revenue,* 697 F.3d 104, 109 (2d Cir. 2012) (explaining that when an agency must resolve a statutory ambiguity, to do so ''with the aid of reliable legislative history is rational and prudent'' (quoting Robert A. Katzman, Madison Lecture: Statutes, 87 N.Y.U. L. Rev. 637, 659 (2012)).

[64] S. Rep. No. 97–384, at 44 (1982).

CEA ''to clarify and strengthen the Commission's authority in this area,'' including authorizing the Commission to prosecute violations of exchange-set limits as if they were violations of the CEA.[65] Thus, by granting the Commission explicit authority to enforce the Commission-mandated exchange-set limits, Congress in effect ratified the 1981 rule, finding it reasonable to impose position limits on an across-the board basis, rather than following a commodity-by-commodity determination. This contributes to the Commission's judgment that Congress reasonably could have followed a similar approach here and, for the reasons given elsewhere, likely did.

c. Comments [66]

i. *Commission's Experience:* No commenter disputed the depth or breadth of the Commission's experience and expertise with position limits.[67] Most, if not all, commenters, many of them exchanges, traders, and other market participants who have been subject to a long-standing federal and exchange-set limit regime, implicitly or explicitly agreed that at least spot-month position limits continue to be essential to prevent manipulation and excessive volatility and thus serve the public interest.[68] One commenter acknowledged that only the Commission can impose and monitor limits across exchanges.[69] Another opined that only the Commission could impose limits without any conflicts of interest due to the exchanges' imperative to maximize trading volume in order to maximize profit.[70]

ii. *Time to Establish Limits:* No commenters disputed the fact that it took many months for the Commission to make a necessity determination before establishing limits. Some commenters agreed with the determinations the Commission preliminarily drew from its experience.[71]

Several commenters asserted that the Commission's reliance on the timelines to support its view ignores other qualifying language in the statute, such as the terms ''necessary'' and ''appropriate.'' [72] The Commission disagrees, because its interpretation of the statute considers the relevant provisions as an integrated whole, which is required in interpreting any statute. Under this approach, it is appropriate to give consideration to the import of the tight statutory deadlines in light of the Commission's experience that it could not possibly comply with if it had to make necessity findings as it has in the past. These comments fail to take these considerations into account. The Commission addresses the language relied upon by these commenters, infra, in its discussion of the text of the statute.

CME also contended that the 180- and 270-day time limits were a difficulty manufactured by the December 2013 Position Limits Proposal itself. According to CME, the Commission could instead expedite the process for setting limits by utilizing its exchanges and others to determine whether position limits are necessary and appropriate for a particular commodity and, if so, the appropriate types and levels of limits and related exemptions.[73] While this is a plausible approach to generating necessity findings, the Commission views it unlikely that Congress had this approach in mind. The provisions at issue make no mention of exchange-set limits or necessity findings. CME also gave no reason to believe that commodity-by-commodity necessity findings could be made by the exchanges within the prescribed 180/270 day limits.

iii. *1981 Rulemaking:* Some commenters disagreed with the Commission's consideration of the 1981 Rule. CME commented that the 1981 Rule is inapposite because there the Commission was requiring DCMs to impose position limits based on an ''antecedent judgment'' that limits were necessary and appropriate; a necessity finding was not required there.[74] The Commission believes that CME's observation is consistent with its interpretation. In the 1981 rule, the Commission made an antecedent judgment on an across-the-board basis that position limits were necessary, and the exchanges then set them according to specific standards. Here, Congress has made the antecedent judgment on an across-the-board basis that position limits are necessary for physical commodities (*i.e.,* commodities other than excluded commodities), and ordered the Commission to set them according to the same types of standards referenced in the 1981 rule. This supports, rather than undermines, the Commission's interpretation that the ''standards'' in CEA section 4a(a)(1), referred to in CEA section 4a(a)(2) as added by the Dodd-Frank Act, are the flexibility and aggregation standards, much as they were in the 1981 rulemaking interpreting CEA section 4a(a)(1).

Several commenters contended that the Commission's reliance on the 1981 rulemaking ignores that the CFTC then imposed limits only after a fact-intensive inquiry into the characteristics of individual contracts markets to determine the limits most appropriate for individual contract markets.[75] However, the Commission has taken those inquiries into account. The Commission believes these inquiries are significant because while the Commission performed such investigation for some markets, it did not do so for all markets ultimately within the scope of the rule. The 1981 Rule directed exchanges to impose limits on *all* futures contracts for which exchanges had not already imposed limits. For example, citing a then-recent disruption in the silver market, the Commission directed that position limits be imposed prophylactically for all futures and options contracts.[76] It further directed the exchanges to consider the characteristics of particular contracts and markets in determining *how* to set limits (the standards, limit

[65] *Id.*

[66] A list is provided below in Section V, Appendix B, of the full names, abbreviations, dates and comment letter numbers for all comment letters cited in this rulemaking. The Commission notes that many commenters submitted more than one comment letter. Additionally, all comment letters that pertain to the December 2013 Position Limits Proposal and the 2016 Supplemental Position Limits Proposal, including non-substantive comment letters, are contained in the rulemaking comment file and are available through the Commission's Web site at *http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1708.* A search can be done online for a particular comment letters by inserting the specific comment letter number in the address in place of the hash tags in the following web address: *http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=#####&SearchText.*

[67] One commenter questioned whether the Commission's experience was even relevant. This commenter asserted that the statute clearly and unambiguously does not mandate imposition of position limits, and therefore no consideration or deference to the Commission's experience is appropriate. CL–ISDA/SIFMA–59611 at 7. But the district court disagreed and directed the Commission to employ its experience in resolving the ambiguities in the statute. 887 F. Supp. 2d at 270, 280–82. In any event, for the reasons discussed, the Commission's reading is, at a minimum, reasonable.

[68] *E.g.,* CL–CME–59718 at 2; *see also* CL–ISDA/SIFMA–59611 at 3, 27–32, App. A at 11, App. B at 6 (arguing for alternatives to limits *outside* the spot month).

[69] CL–CME–59718 at 18.

[70] CL–CMOC–60400 at 3; and CL-Public Citizen-60390 at 2–3.

[71] *E.g.,* CL–A4A–59714 at 3.

[72] CL–CME–59718 at 7; and CL–ISDA/SIFMA–59611 at 9, n. 32 (asserting that deadlines are no excuse for the Commission to be ''arbitrary'' or ''sloppy.'').

[73] CL–CME–59718 at 7.

[74] *Id.* at 9–10.

[75] CL–AMG–59709 at 4, n. 8; and CL–CME–59718 at 15–16.

[76] Establishment of Speculative Position Limits, 46 FR at 50940–41 (Oct. 16, 1981).

levels and so on) but not whether to do so.[77] It specifically rejected commenters' concerns that position limits would not be beneficial for all contracts, finding, after ''considerable years of Federal and contract market regulatory experience,'' that ''the capacity of any contract market . . . is not unlimited,'' and there was no need to evaluate the particulars of whether any contract would benefit from position limits.[78] The Dodd-Frank Act amendments unfolded in an analogous fashion. Prior to the Dodd-Frank Act, Congress conducted studies of some, but not all, markets in physical commodities. This history suggests that Congress extrapolated from the conclusions reached in those studies to determine that position limits were necessary for all physical commodities other than excluded commodities.

ISDA and SIFMA asserted that the Commission's reliance on the 1981 rulemaking is unavailing because (1) it cannot alter the Commission's statutory burdens with respect to imposing position limits; and (2) it was never adopted by Congress.[79] The first of these comments begs the question, *i.e.,* what is ''the statutory burden'' intended in the text of CEA sections 4a(a)(1) and (2), read as a whole and considered in context to resolve the ambiguity found by the district court. As to the second comment, the Commission does not contend that Congress adopted the 1981 rule. Rather, it is relevant because the language the district court found ambiguous in the Dodd-Frank Act amendments to CEA section 4a(a) resembles the language of the 1981 rule, and some of the context is parallel. The relevance of this rulemaking is supported by the fact that Congress did ratify it the following year, when it amended the CEA by granting the Commission the authority to enforce the position limits set by the exchanges, reinforcing that as a historical matter Congress had approved an omnibus prophylactic approach as reasonable. That Congress had approved of such an approach before and then used language in the Dodd-Frank Act that closely resembles the very language the Commission used when it mandated that omnibus approach is another factor that weighs on the side of interpreting the statutory ambiguity to find a mandate to impose physical commodity positon limits.[80]

Finally, several commenters asserted that the Commission cannot consider the 1981 rulemaking because the Commission later allowed exchanges to set position accountability levels in lieu of limits for some commodities and contracts.[81] Those later exemptions do not, however, alter the language or import of the 1981 rule, which directed the exchanges to impose limits in accordance with ''standards'' that did not include a necessity finding. The 1981 rulemaking is the last time the Commission definitively addressed and identified the ''standards'' in CEA section 4a(a)(1) for imposing across-the-board, prophylactic position limits in a manner akin to the Dodd-Frank Act amendments. That other approaches intervened is not inconsistent with the inference that Congress was influenced by the 1981 rulemaking in the Dodd-Frank Act amendments.

4. Legislative History of the Dodd-Frank Act Amendments to Position Limits Statute

As discussed in the 2016 Supplemental Position Limits Proposal, the Commission has also considered the legislative history of the Dodd-Frank Act amendments.[82] That history contains further indication that Congress intended to mandate the imposition of limits for physical commodity derivatives without requiring the Commission to make antecedent necessity findings, and did not intend the term ''standards'' to include such a finding.[83]

The Commission's preliminary interpretation of CEA section 4a(a)(2) is based in part on congressional concerns that arose, and congressional actions taken, before the passage of the Dodd-Frank Act amendments.[84] During the 1990s, the Commission began permitting exchanges to experiment with an alternative to position limits—position accountability, which allowed a trader to hold large positions subject to reporting requirements and gave the exchange the right to order the trader to hold or reduce its position.[85] Then, in the Commodity Futures Modernization Act of 2000 (''CFMA''),[86] Congress expressly authorized the use of position accountability as an alternative means to limit speculative positions.[87]

Following this experiment with position accountability, Congress became concerned about fluctuations in commodity prices. In the late 1990s and 2000s, Congress conducted several investigations that concluded that excessive speculation accounted for significant volatility and price increases in physical commodity markets. For example, a congressional investigation determined that prices of crude oil had risen precipitously and that ''[t]he traditional forces of supply and demand cannot fully account for these increases.'' [88] The investigation found evidence suggesting that speculation was responsible for an increase of as much as $20–25 per barrel of crude oil, which was then at $70.[89] Subsequently, Congress found similar price volatility stemming from excessive speculation in the natural gas market.[90]

These investigations appear to have informed the drafting of the Dodd-Frank Act. During hearings prior to the passage of the Dodd-Frank Act, Senator Carl Levin, then-Chair of the Senate Permanent Subcommittee on Investigations that had conducted them, urged passage to ensure ''a cop on the beat in all commodity markets where U.S. commodities are traded . . . that can enforce the law to prevent excessive speculation and market manipulation.'' [91] In addition, Congress viewed the nearly $600 trillion little-regulated swaps market as a ''major contributor to the financial crisis'' because excessive risk taking, hidden leverage, and under collateralization in that market created a systemic risk of harm to the entire financial system.[92] As Senator Cantwell and others explained, it was imperative that the CFTC have the ability to regulate swaps through

[77] *Id.*

[78] *Id.*

[79] CL–ISDA/SIFMA–59611 at 9.

[80] *CFTC* v. *Schor,* 478 U.S. 833, 846 (1986).

[81] *E.g.,* CL–ISDA/SIFMA–59611 at 9; and CL–AMG–59709 at 4, n.8.

[82] *Union Carbide Corp. & Subsidiaries* v. *Comm'r of Internal Revenue,* 697 F.3d 104, 109 (2d Cir. 2012) (explaining that when an agency must resolve a statutory ambiguity, to do so ''with the aid of reliable legislative history is rational and prudent'' (quoting Robert A. Katzman, Madison Lecture: Statutes, 87 N.Y.U. L. Rev. 637, 659 (2012)).

[83] December 2013 Position Limits Proposal, 78 FR at 75682, 75684–85.

[84] *Id.* at 75682.

[85] Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations, 75 FR 4144, 4147 (Jan. 26, 2010); Revision of Federal Speculative Position Limits and Associated Rules, 64 FR 24038, 24048–49 (May 5, 1999).

[86] Commodity Futures Modernization Act of 2000, Public Law 106–554, 114 Stat. 2763 (Dec. 21, 2000).

[87] 7 U.S.C. 7(d)(3) (2009).

[88] *The Role of Market Speculation in Rising Oil and Gas Prices: A Need to Put the Cop Back on the Beat,* Staff Report, Permanent Subcommittee on Investigations of the Senate Committee on Homeland Security and Governmental Affairs, U.S. Senate, S. Prt. No. 109–65 at 1 (June 27, 2006).

[89] *Id.* at 12; *see also Excessive Speculation in the Natural Gas Market,* Staff Report, Permanent Subcommittee on Investigations of the Senate Committee on Homeland Security and Governmental Affairs, U.S. Senate at 1 (June 25, 2007), *available at http://www.levin.senate.gov/imo/media/doc/supporting/2007/PSI.Amaranth.062507.pdf* (last visited Mar. 18, 2013) (''Gas Report'').

[90] Gas Report at 1–2.

[91] 156 Cong. Record S. 4064 (daily ed. May 20, 2010).

[92] S. Rep. 111–176, at 29 (2010).

''position limits,'' ''exchange trading,'' and ''public transparency'' to avoid a recurrence of the instability that rippled through the entire financial system in 2008.[93] And in the House of Representatives, Representative Collin Peterson, then-Chairman of the House Committee on Agriculture and author of an amendment strengthening the position limits provision as discussed below, reminded his colleagues that his committee's own ''in-depth review of derivative markets began when we experienced significant price volatility in energy futures markets due to excessive speculation—first with natural gas and then with crude oil. We all remember when we had $147 oil. . . . This conference report [now] includes the tools we authorized and the *direction* to the CFTC to mitigate outrageous price spikes we saw 2 years ago.'' [94] Congress's focus in its investigations on excessive speculation involving physical commodities is reflected in the scope of the Dodd-Frank Act's position limits amendment: It applies only to physical commodities.

The evolution of the position limits provision in the bills before Congress from permissive to mandatory supports a preliminary determination that Congress intended to do something more than continue the long-standing statutory regime giving the Commission discretionary authority to impose limits.[95] As initially introduced, the House bill that became the Dodd-Frank Act provided the Commission with discretionary authority to issue position limits, stating that the Commission ''may'' impose them.[96] However, the House replaced the word ''may'' with the word ''shall,'' suggesting a specific judgment that the limits should be mandatory, not discretionary. The House also added other language militating in favor of interpreting CEA section 4a(a)(2) as a mandate. In two new subsections, it set the tight deadlines described above.[97] After changing ''may'' to ''shall,'' the House further amended the bill to refer in one instance to the limits for agricultural and exempt commodities as ''required.'' [98] And only after the language had changed from permissive to mandatory, the House added the requirement that the Commission conduct studies on the ''effects (if any) of position limits imposed'' [99] to determine if the required position limits were harming U.S. markets.[100] Underscoring its intent to amend the bill to include a mandate, the House Report accompanying the House Bill stated that it ''required'' the Commission to impose limits.[101] The Conference Committee adopted the House bill's amended provisions on position limits and then strengthened them even further by referring to the position limits as ''required'' an additional three times, bringing the total to four times in the final legislation the number of references in statutory text to position limits as ''required.'' [102]

a. Comments

A number of commenters generally supported or opposed the Commission's consideration of Congressional investigations and the textual strengthening of the Dodd-Frank bill. The Commission addresses specific comments below.

i. *Congressional Investigations:* Several commenters agreed that the Congressional investigations, hearings and reports support the view that Congress decided to mandate position limits.[103] They pointed out that Congress's investigations followed amendments in 2000 to the CEA as part of the CFMA that exempted swaps and energy derivatives from position limits and expressly authorized exchanges to impose position accountability levels in lieu of limits.[104] According to the Commodity Markets Oversight Coalition (''CMOC''), ''witnesses confirmed [at those hearings] that the erosion of the position limits regime was a leading cause in market instability and wild price swings.'' [105] Senator Levin, who presided over the investigations, commented that those investigations, conducted from 2002 onwards, ''into how our commodity markets function, focusing in particular on the role of excessive speculation on commodity prices'' ''have demonstrated that the failure to impose and enforce effective position limits have led to greater speculation and increased price volatility in U.S. commodity markets.'' [106] According to Senator Levin, the investigations ''provide[d] strong support for the Dodd-Frank decision to require the Commission to impose position limits on all types of commodity futures, swaps, and options.'' [107] Senator Levin also stated that the harms of excessive speculation continue to be felt in the absence of the mandated limits. He cited recent actions by federal regulators to stop manipulation in energy markets, and opined that the continuing problems in the absence of the mandated limits only reinforce the reasonableness of the Commission's view that Congress intended to mandate position limits as a prophylactic measure.[108] Senator Levin's point was echoed by Public Citizen, a consumer advocacy organization, and Airlines for America, a trade association for the U.S. scheduled airline industry.[109]

Other commenters disagreed with the Commission's preliminary determination that the Congressional investigations indicate that Congress intended to mandate limits. CME asserted that the investigations do not in themselves demonstrate that Congress required the CFTC to impose position limits as recommended even if those investigations suggest that excessive speculation poses a burden on interstate commerce in certain physical commodity markets.[110] Citadel questioned whether the cited reports could be ''broadly indicative of Congressional intent,'' or could ''redefine statutory language that has existed for nearly eight decades.'' [111]

But the Commission is not relying solely on these reports. The question, rather, is whether these Congressional

[93] *See, e.g.,* 156 Cong. Rec. S 2676–78, S 2698–99, S 3606–07, S 3966, S 5919 (daily ed. April 27, May 12, 19, July 15, 2010 (providing statements of Senators Cantwell, Feinstein, Lincoln)).

[94] 156 Cong. Rec. H5245 (daily ed. June 30, 2010) (emphasis added).

[95] December 2013 Position Limits Proposal, 78 FR at 75684–85.

[96] Initially, the House used the word ''may'' to permit the Commission to impose aggregate positions on contracts based upon the same underlying commodity. *See* H.R. 4173, 11th Cong. 3113(a)(2) (providing the version introduced in the House, Dec. 2, 2009) (''Introduced Bill''); *see also* Brief of Senator Levin et al as *Amicus Curiae* at 10–11, *ISDA* v. *CFTC,* no. 12–5362 (D.C. Cir. Apr. 22, 2013), Document No. 1432046 (hereafter ''Levine Br.'').

[97] Levin Br. at 11 (citing H.R. 4173, 111th Cong. 3113(a)(5)(2), (7) (as passed by the House Dec. 11, 2009) (''Engrossed Bill'')).

[98] *Id.* at 12. (citing Engrossed Bill at 3113(a)(5)(3)).

[99] 15 U.S.C. 8307; Engrossed Bill at 3005(a).

[100] *See* Levin Br. at 13–17; *see also* DVD: October 21, 2009 Business Meeting (House Agriculture Committee 2009), *ISDA* v. *CFTC,* Dkt. 37–2 Exh. B (Apr. 13, 2012) at 59:55–1:02:18.

[101] Levin Br. at 23 (citing H.R. Rep. No. 111–373 at 11 (2009)).

[102] Levin Br. at 17–18.

[103] CL–CMOC–59720 at 2; CL–Sen. Levin–59637 at 2–5; and CL–A4A–59686 at 2–3.

[104] CL–IECA–59964 at 2; CL–A4A–59686 at 2; and CL–Public Citizen–59648 at 2–3.

[105] CL–CMOC–59720 at 2.

[106] CL–Sen. Levin–59637 at 3–4.

[107] *Id.*

[108] *Id.* at 2.

[109] CL–Public Citizen–59648 at 2–3, and CL–A4A–59686 at 1–2.

[110] CL–CME–59718 at 8. CME also asserted that the Congressional investigation into excessive speculation in natural gas futures focused more on the fact that position accountability rules for exchange-traded natural gas futures were not in place for ''look-alike'' natural gas swaps traded ''over the counter,'' permitting regulatory arbitrage.

[111] CL–Citadel–59717 at 3.

investigations and findings of excessive speculation and price volatility in energy markets, conducted and issued when the Commission was authorized but not required by law to impose limits, may be one indication, among others, that Congress sought to do something more with the Dodd-Frank Act amendments than to maintain the statutory status quo for futures on physical commodities. In the Commission's preliminary view, it is more plausible, based on these investigations, that Congress sought to do something more—to require that the Commission impose limits for the covered commodities without having to first find that they are necessary to prevent excessive speculation. Contrary to Citadel's comment, the Commission is not relying on the investigations and reports to redefine statutory language that has existed for nearly eight decades. Rather, the Commission believes that the investigations favor the conclusion that Congress added CEA section 4a(a)(2) to the pre-existing language in order to strengthen the long-standing position limits regime for a category of commodity derivatives—physical commodities—that Congress's investigations revealed to be vulnerable to substantial price fluctuations.

ii. *Evolution of the Dodd-Frank Bill:* Several commenters agreed with the Commission's preliminary determination that the strengthening of the position limits language in the Dodd-Frank bill evinces Congress' intent to mandate limits.[112]

CME and MFA disagreed; while they do not directly address this point, they believed that the strengthening of the language in the Dodd-Frank bills does not indicate that Congress intended to de-couple the enacted directive to impose position limits from the necessity finding of CEA section 4a(a)(1).[113] The Commission, however, preliminarily considers this the most plausible interpretation. The evolution of the bill from one stating the Commission ''may'' impose position limits to include statements that the Commission ''shall'' impose them, that they are ''required,'' and that the Commission shall study their effects indicates intentional progressive refinement from a bill that would continue the status quo for futures to one that added special nondiscretionary requirements for a category of commodities. This legislative evolution also supports the conclusion ''standards'' does not include an antecedent necessity finding.

5. The Commission Preliminarily Interprets the Text of CEA Section 4a(a) as an Integrated Whole, In Light of Its Experience and Expertise.

In the December 2013 Position Limits Proposal, the Commission discussed how its interpretation of the text of CEA section 4a(a), considered as an integrated whole, is consistent with and supports its conclusions based on experience and expertise. As discussed, the ambiguity is the meaning of CEA section 4a(a)(2)'s statement that the Commission ''shall'' establish limits on physical commodities other than excluded commodities ''[i]n accordance with the standards'' set forth in CEA section 4a(a)(1). If ''standards'' includes a necessity finding, then a necessity finding is required before limits can be imposed on agricultural and exempt commodities. If not, the Commission must impose limits for that subset of commodity derivatives. In the December 2013 Position Limits Proposal, the Commission resolved the ambiguity by preliminarily determining that the reference in CEA section 4a(a)(2) to the ''standards'' in pre-Dodd-Frank section 4a(a)(1) refers to the criteria in CEA section 4a(a)(1) for *how* the required limits are to be set and not the antecedent finding *whether* limits are even necessary. The Commission explained that, in its preliminary view, ''standards'' refers to, in CEA section 4a(a)(1), only the following two provisions. First, the limits must account for situations in which one person controls another or two persons act in concert, by aggregating those positions as if the trading were done by one person acting alone (aggregation). The second ''standard'' in CEA section 4a(a)(1) states that the limits may be different for different commodities, markets, delivery months, etc. (flexibility).

The Commission reasoned that this construction of ''standards'' seemed most consistent with the Commission's experience and history administering position limits. It also seemed most consistent with the text of CEA section 4a(a)(2), the rest of CEA section 4a(a), and the Act as a whole. The Dodd-Frank Act amendments to CEA section 4a(a) largely re-shape CEA section 4a(a) by adding a new, detailed, and comprehensive section 4a(a)(2) that applies only to a subset of the derivatives regulated by the Commission—physical commodities like wheat, oil, and gold—and not intangible commodities like interest rates. Amended CEA section 4a(a) repeatedly uses the word ''shall'' and refers to the new limits as ''required,'' differentiating it from the text that existed before the Dodd-Frank Act.[114] Never before in the Commission's experience had Congress set deadlines on action for position limits by a date certain, much less the short time provided in CEA section 4a(a)(2)(B).[115] Nor, in the Commission's experience, had Congress required a report by a given date or committed itself to hold hearings on the report within 30 days thereafter.[116] The Commission preliminarily concluded that, considered as a whole in light of this experience, these provisions evince a Congressional mandate that the Commission impose limits on physical commodities, that it do so quickly, that it impose limit levels in accordance with certain requirements, and that it study the effectiveness of the limits *after* imposing them and then report to Congress.

By the same token, the Commission preliminarily determined that interpreting CEA section 4a(a)(2) as it proposed to do would not render superfluous the necessity finding requirement in CEA section 4a(a) because that section still applies to the non-physical (excluded) commodity derivatives that are not subject to CEA section 4a(a)(2). Nor would it nullify other parts of CEA section 4a(a), as those are unaffected by this reading.

The Commission received a number of comments on its discussion of the interplay between the statute's text and the Commission's experience and expertise. The Commission has considered them carefully, but is not thus far persuaded. The Commission preliminarily believes that it is a reasonable interpretation of the text of the statute considered as an integrated whole and viewed through the lens of the Commission's experience and expertise, that Congress mandated that the Commission establish position limits for physical commodities. It is also reasonable to construe the reference to ''standards'' as an instruction to the Commission to apply the flexibility and aggregation standards set forth in CEA section 4a(a)(1), just as the Commission instructed the exchanges to impose

[112] CL–Public Citizen–59648 at 2.

[113] CL–CME–59718 at 2, 5–12 (maintaining statutory language requires necessity finding); and CL–MFA–59606 at 9 (citing S. Rept. 111–176 (Apr. 30, 2010, which states ''[t]his section authorizes the CFTC to establish aggregate position limits. . . .'').

[114] *E.g.,* CEA sections 4a(a)(2)(A) (providing that the Commission ''shall'' set the limits); 4a(a)(2)(B) (referring twice to the ''limits required'' and directing that they ''shall'' be established by a time certain); 4a(a)(3)(referring to the limits ''required'' under subparagraph (A)); 4a(a)(5)(stating that the Commission ''shall'' concurrently establish limits on economically equivalent contracts).

[115] 7 U.S.C. 6a(a)(2(B).

[116] 15 U.S.C. 8307.

omnibus limits in 1981. And it is at least reasonable to conclude that Congress, in directing the Commission to impose the ''required'' limits on extremely tight deadlines, did not intend the Commission to independently make an antecedent finding that any given position limit for physical commodities is ''necessary''—a finding that would take many months for each individual physical commodity contract.

a. Comments

Several commenters disputed the Commission's interpretation, based on its experience and expertise, that CEA section 4a(a)(2) is a mandate for prophylactic limits based on their view that the statute unambiguously requires the Commission to promulgate position limits only after making a necessity finding, and only ''as appropriate.'' [117] But in *ISDA* v. *SIFMA,* the district court held that the statute was ambiguous in this respect, and the Commission here is following the court's direction to apply its experience and expertise to resolve the ambiguity. This is consistent with a commenter's statement that ''the meshing of the Dodd-Frank Act into the CEA may have created some ambiguity from a technical drafting/wording standpoint.'' [118] Nevertheless, the Commission addresses these textual arguments to show that its preliminary interpretation is, at a minimum, a permissible one.

The commenters that disagreed with the Commission's preliminary conclusion argued that the Commission: (i) Erred in determining that the reference to ''standards'' in CEA section 4a(a)(2) does not include the necessity finding in CEA section 4a(a)(1); (ii) failed to consider other provisions that show Congress intended to require the Commission to make antecedent findings; and (iii) incorrectly determined that its interpretation is the only way to give effect to CEA section 4a(a)(2).

i. *Meaning of Standards:* Several commenters asserted that the language: ''[in] accordance with the standards set forth in paragraph (1)'' in section 4a(a)(2) must include the phrase ''as the Commission finds are necessary to diminish, eliminate, or prevent [the burden on interstate commerce]'' in CEA section 4a(a)(1).[119] They believed that the Commission's contrary interpretation constitutes an implied repeal of the necessity finding language.[120]

The Commission disagrees that this constitutes an implied repeal. First, CEA section 4a(a)(2) applies only to physical commodities, not other commodities. Accordingly, the requirement of a necessity finding in section 4a(a)(1) still applies to a broad swath of commodity derivatives. Second, there is no implied repeal even in part, because the Commission is interpreting express language—the term ''standards.'' The Commission must bring its experience to bear when interpreting the ambiguity in the new provision, and the Commission preliminarily believes that the statute, read in light of the Commission's experience administering position limits and making necessity findings, is more reasonably read as an express limited exception, for physical commodities futures and economically equivalent swaps, to the preexisting authorization in CEA section 4a(a)(1) for the Commission to impose limits when it finds them necessary.

ii. *Other Limiting Language:* Some commenters pointed to a number of terms and provisions that they say support the notion that the Commission must make antecedent findings before imposing any limits under new CEA section 4a(a)(2).

First, some commenters asserted that the term ''as appropriate'' in CEA sections 4a(a)(3) (factors that the ''Commission, ''as appropriate'' must consider when it ''shall set limits'') and 4a(a)(5)(A) (providing that Commission ''shall'' ''as appropriate'' establish limits on swaps that are economically equivalent to physical commodity futures and options) require the Commission to make antecedent findings that the limits required under CEA section 4a(a)(2) are appropriate before it may impose them.[121] The district court found these words to be ambiguous. In the court's view, they could refer to the Commission's obligation to impose limits (*i.e.,* the Commission shall, ''as appropriate,'' impose limits), or to the level of the limits the Commission is to impose.[122]

The Commission preliminarily believes that when these words are considered in the context of CEA section 4a(a)(2)–(7) as a whole, including the multiple uses of the new terms ''shall'' and ''required'' and the historically unique stringent time limits for imposing the covered limits and post-imposition study requirement, it is more reasonable to interpret these words as referring to the level of limits, *i.e.,* the Commission must set physical commodity limits at an appropriate level, and not to require the Commission to first determine whether the required limits are appropriate before it may even impose them.[123] In other words, while Congress made the threshold decision to impose position limits on physical commodity futures and options and economically equivalent swaps, Congress at the same time delegated to the Commission the task of setting the limits at levels that would maximize Congress' objectives.

Some commenters claimed that other parts of CEA section 4a(a)(2) undermine the Commission's determination. First, CEA section 4a(a)(2)(C) states that the ''[g]oal . . . [i]n establishing the limits required'' is to ''strive to ensure'' that trading on foreign boards of trade (''FBOTs'') for commodities that have limits will be subject to ''comparable limits.'' It goes on to state that for ''any limits to be imposed'' the Commission will strive to ensure that they not shift trading overseas. Commenters argue that ''any limits to be imposed'' under CEA section 4a(a)(2)(A) implies that limits might not be imposed under that section. However, in the context discussed and in view of the reference in that section to position limits

[117] CL–CME–59718 at 11; CL–MFA–59606. at 9; etc. *But see, e.g.,* CL–A4A–59714 at 2–3 (noting that notwithstanding the ''meshing'' problems, ''it is clear that the Commission's interpretation is reasonable and fully supported by the context in which the Dodd-Frank Act was passed, its legislative history, and the many other factors identified in the NPRM''); CL–AFR–59685 at 1; CL–Public Citizen–60390 at 2; CL–Public Citizen–59648 at 2; CL–Sen. Levin–59637 at 4; and CL–CMOC–59720 at 2–3.

[118] CL–A4A–59714 at 2–3.

[119] *See, e.g.,* CL–CME–59718 at 12–13; CL–Citadel–59717 at 3–4; CL–AMG–59709 at 3; CL–MFA–59606 at 9–10; CL–ISDA/SIFMA–59611 at 5–7; CL–IECAssn–59679 at 3–4; and CL–FIA–59595 at 6–7.

[120] CL–CME–59718 at 2, 12 (citing *Hunter* v. *FERC,* 711 F.3d 155 (D.C. Cir. 2013)).

[121] *See, e.g.,* CL–ISDA/SIFMA–59611 at 5, 7–8 (citing CEA section 4a(a)(5) as authorizing aggregate position limits ''as appropriate'' for swaps that are economically equivalent to DCM futures and options and CEA section 4a(a)(3), which directs the Commission to set position limits as appropriate and to the maximum extent practicable, in its discretion: (i) To diminish, eliminate, or prevent excessive speculation; (ii) to deter and prevent market manipulation, squeezes, and corners; (iii) to ensure sufficient market liquidity for bona fide hedgers; and (iv) to ensure that the price discovery function of the underlying market is not disrupted.).

[122] 887 F.Supp. 2d at 278; December 2013 Position Limits Proposal, 78 FR at 75685, n. 59.

[123] CEA section 4a(a)(2)(A) provides that the Commission ''shall'' establish limits; CEA section 4a(a)(2)(B) refers multiple times to the ''required'' limits in (A) that ''shall'' be established within 180 or 270 days of enactment of Dodd-Frank; and CEA section 4a(a)(2)(C) provides that ''[i]n establishing the limits required'' the Commission shall ''strive to ensure'' that trading on foreign boards of trade for commodities that have limits will be subject to ''comparable limits,'' thereby assuming that limits must be established and requiring that they be set at levels in accordance with particular considerations. CEA section 4a(a)(3) contains ''specific limitations'' on the ''required'' limits which are most reasonably understood to be considerations for the Commission for the levels of limits.

''required,'' the reference to ''any limits to be imposed'' refers again to the levels or other standards applied. That is, whatever the contours the Commission chooses for the required limits, they must meet the goal set forth in that section.

Second, CEA section 4a(a)(3)(B) states certain factors that the Commission must consider in setting limits under CEA section 4a(a)(2).[124] The Commission sees no inconsistency with mandatory position limits—the Commission must consider these factors in setting the appropriate levels and other contours. Indeed, CEA section 4a(a)(3)(B) applies by its own terms to ''establishing the limits required in paragraph (2).'' Moreover, consideration of these factors under CEA section 4a(a)(3) is not mandatory, as some commenters suggest,[125] but rather to be made ''in [the Commission's] discretion.'' [126] In the Commission's preliminary view, there is thus nothing in these provisions at odds with the Commission's interpretation that it is required by CEA section 4a(a)(2)(A) to impose limits on a subset of commodities without making antecedent findings whether they should be imposed, particularly when the language at issue is construed, as it should be, with other terms in CEA section 4a(a)(2)–(7), discussed above, that use mandatory language and impose time limits.

Some commenters stated that two pre-Dodd Frank Act provisions in CEA section 4a undermine the Commission's interpretation. The first is CEA section 4a(e),which states, ''if the Commission shall have fixed limits . . . for any contract . . . , then the limits'' imposed by DCMs, SEFs or other trading facilities ''shall not be higher than the limits fixed by Commission.'' [127] According to a commenter, the ''if/then'' formulation suggests position limits should not be presupposed for any contract.[128] The Commission sees the provision differently. CEA section 4a(a)(2) applies only to a subset of futures contracts—contracts in physical commodities. For other commodities, position limits remain subject to the Commission's determination of necessity, and the ''if/then'' formulation applies and remains logical. There is, accordingly, no inconsistency.

The second pre-Dodd Frank Act provision the commenters mentioned is CEA section 5(d)(5); [129] it gives the exchanges discretionary authority to impose position limits on all commodity derivatives ''as is necessary and appropriate.'' [130] There is, however, no inconsistency. Exchanges retain the discretionary authority to set position limits for the many commodities not covered by CEA section 4a(a)(2), and they retain the discretion to impose position limits for physical commodities, so long as the limits are no higher than federal position limits.

Some commenters cited other language in CEA section 5(d)(5) to support their assertion that, notwithstanding the Dodd-Frank Act amendments discussed above requiring the Commission to impose limits, the Commission retains and should exercise its discretion to impose position accountability levels in lieu of limits or delegate that authority exchanges to do so. CEA section 5(d)(5) authorizes exchanges to adopt ''position limitations or position accountability'' levels in order to reduce the threat of manipulation and congestion. These commenters also pointed out that the Commission has previously endorsed accountability levels for exchanges in lieu of limits.[131] Other commenters disagree. They asserted that, given what they interpret as a mandate in CEA section 4a(a)(2) for the Commission to impose position limits for physical commodities, it would be inappropriate for the Commission to consider imposing position accountability levels instead for those commodities, or to allow exchanges to do so.[132]

The Commission agrees with the latter group of commenters and finds the former reading strained. CEA section 4a(a)(2) makes no mention of position accountability levels. Regardless whether pre-Dodd Frank section 5(d)(5) allows exchanges to set accountability levels in lieu of limits where the Commission has not set limits, and regardless whether the Commission has in the past endorsed exchange-set position accountability levels in lieu of limits, CEA section 4a(a)(2) does not mention that tool. If anything, reference to accountability levels elsewhere in the CEA shows that Congress understands that exchanges have used position accountability, but made no reference to it in amended CEA section 4a(a).

iii. *Avoiding Surplusage or Nullity:* Several commenters took issue with the Commission's preliminary determination that its interpretation is necessary in order to avoid rendering CEA section 4a(a)(2)(A) surplusage. These commenters suggested that reading the term ''standards'' in CEA section 4a(a)(2)(A) to include the antecedent necessity finding in CEA section 4a(a)(1) will not render CEA section 4a(a)(2) surplusage because if the Commission finds a position limit is ''necessary'' and ''appropriate,'' it now must impose one (as opposed to pre-Dodd-Frank, when the Commission had authority but not a mandate under CEA section 4a(a) to impose limits).[133] The Commission finds this reading highly unlikely. There is no history of the Commission determining that limits are necessary and appropriate, but then declining to impose them. Nor is it reasonable to expect that the Commission might do so. Indeed, historically necessity findings were made only in connection with establishing limits.

Furthermore, if Congress had still wanted to leave it to the Commission to ultimately decide whether a limit was necessary, there is no reason for it to have also set tight deadlines, repeat multiple times that the limits are ''required,'' and direct the agency to conduct a study after the limits were imposed. In other words, requiring the Commission to make an antecedent necessity finding would render many of the Dodd-Frank Act amendments superfluous. For example, if the Commission determined limits were not necessary then, contrary to CEA section 4a(a)(2), no limits were in fact ''required,'' no limits needed to be imposed by the deadlines, and no study

[124] *See, e.g.,* CL–CME–59718 at 11, 13–17, and CL–FIA–59595 at 5–6.

[125] *See, e.g.,* CL–AMG–59709 at 3; and CL–CME–59718 at 13–17.

[126] CEA section 4a(a)(3), 7 U.S.C. 6a(a)(3).

[127] CEA section 4a(e), 7 U.S.C. 6a(e).

[128] CL–CME–59718 at 10 (citing CEA section 4a(e)).

[129] 7 U.S.C. 7(d)(5).

[130] CL–CME–59718 at 11 (citing 7 U.S.C. 7(d)(5)).

[131] CL–CME–59718 at 10; CL–AMG–59709 5–6; CL–FIA–59595 at 12–13; CL–FIA–60392 at 4–6, 8 (asserting that under the Commission's general rulemaking authority in CEA section 8a(5), 7 U.S.C. 12a(5), ''the Commission has the power to adopt, as part of an accountability regime, a rule pursuant to which it or a DCM could direct a market participant to reduce speculative positions above an accountability limit because that authority is 'reasonably necessary to effectuate' a position accountability rule,'' and observing that the Commission previously determined in rulemakings that exchange-set accountability levels represent an alternative means to limit excessive speculation); CL–FIA–60303 at 3–4; CL–DBCS–59569 at 4; CL–MFA–60385 at 7–8, 10–14; and CL–Olam–59658 at 1–2 (declaring that the Commission can and should permit exchanges to administer position accountability levels in lieu of Commission-set limits under CEA section 4a(a)(2)).

[132] CL–Public Citizen–60390 at 3–4 (noting other concerns with exchange set limits or accountability levels); CL–IECA 60389 at 3–4 (asserting that the Commission should not cede its authority to exchanges); CL–AFR–60953 at 4; CL–A4A–59686 at 2–3; CL–IECA–59671 at 2; and CL–CMOC–59720 at 2.

[133] CL–ISDA/SIFMA–59611 at 5; and CL–MFA–59606 at 9–10. The District Court expressed the same concern. 887 F. Supp. 2d at 274–75.

needed to be conducted. But none of these provisions were phrased in conditional terms (*e.g., if* the Commission finds a limit necessary, *then* it shall . . . ). Had Congress wanted the Commission to continue to be the decisionmaker regarding the need for limits, it could have expressed that view in countless ways that would not strain the statutory language in this way.

CME contended that the Commission's position—that requiring a necessity finding would essentially give the Commission the same permissive authority it had before the Dodd-Frank Act amendments—is ''short-sighted'' because other provisions of CEA section 4a(a) ''would still have practical significance.'' In support of this view, CME stated that new CEA sections 4a(a)(2)(C) and 4(a)(3)(B) have significance even if the Commission is required to make a necessity finding because they ''set forth safeguards that the CFTC must balance when it establishes limits'' after ''the CFTC finds that such limits are necessary.'' The Commission preliminarily believes it unlikely that Congress would have intended that. On CME's reading, the statute would place additional requirements to constrain the Commission's *preexisting* authority. Given the background for the amendments, particularly the studies that preceded the Dodd-Frank Act, the Commission sees no reason why Congress would have placed *additional* constraints, nor any reason it would have placed them with respect to physical commodities but not excluded commodities or others. This comment also does not address the thrust of the Commission's interpretation, which is that finding a mandate is the only way to read the entirety of the statute harmoniously, including the timing requirements of CEA section 4a(a)(2)(B) and the reporting requirements of Section 719 of the Dodd-Frank Act, account for the historical context, and, at the same time, avoid reading CEA section 4a(a)(2)(A) as the functional equivalent of CEA section 4a(a)(1).[134] CME also cited CEA section 4a(a)(5), which requires position limits for economically equivalent swaps, to make the same point that there are still meaningful provisions in CEA section 4a(a), even with a necessity finding. But CEA section 4a(a)(1) already authorizes the Commission to establish limits on swaps as necessary, and so the authority, which would be discretionary under CME's reading, to impose limits on economically equivalent swaps would add nothing to the statute and the amendment would be wholly superfluous.

6. Conclusion

Having carefully considered the text, purpose and legislative history of CEA section 4a(a) as a whole, along with its own experience and expertise and the comments on its proposed interpretation, the Commission preliminarily believes for the reasons above that Congress—while not expressing itself with ideal clarity—decided that position limits were necessary for a subset of commodities, physical commodities, mandated the Commission to impose them on those commodities in accordance with certain criteria, and required that the Commission do so expeditiously, without first making antecedent findings that they are necessary to prevent excessive speculation. Consistent with this interpretation, Congress also directed the agency to report back to Congress on their effectiveness within one year. In the Commission's preliminary view, this interpretation, even if not the only possible interpretation, best gives effect to the text and purpose of the Dodd-Frank Act amendments in the context of the pre-existing position limits provision, while ensuring that neither the amendments nor the pre-existing language is rendered superfluous.

### *C. Necessity Finding*

1. Necessity

The Commission reiterates its preliminary alternative necessity finding as articulated in the December 2013 Position Limits Proposal: [135] Out of an abundance of caution in light of the district court decision in *ISDA* v. *CFTC,*[136] and without prejudice to any argument the Commission may advance in any forum, the Commission reproposes, as a separate and independent basis for the Rule, a preliminary finding herein that the speculative position limits in this reproposed Rule are necessary to achieve their statutory purposes.

As described in the Proposal, the policy basis and reasoning for the Commission's necessity finding is illustrated by two major incidents in which market participants amassed massive futures positions in silver and natural gas, respectively, which enabled them to cause sudden and unreasonable fluctuations and unwarranted changes in the prices of those commodities. CEA section 4a(a)(1) calls for position limits for the purpose of diminishing, eliminating, or preventing the burden of excessive speculation.[137] Although both episodes involved manipulative intent, the Commission believes that such intent is not necessary for an excessively large position to give rise to sudden and unreasonable fluctuations or unwarranted changes in the price of an underlying commodity. This is illustrated, for example, by the fact that when the perpetrators of the silver manipulation lost the ability to control their scheme, *i.e.,* to manipulate the market at will, they were forced to liquidate quickly, which, given the amount of contracts sold in a very short time, caused silver prices to plummet. Any trader who was forced by conditions in the market or their own financial condition to liquidate a very large position could predictably have similar effects on prices, regardless of their motivation for amassing the position in the first place. Moreover, although these two episodes unfolded in contract markets for silver and natural gas, and unfolded at two different times in the past, there is nothing unique about either market at either relevant time that causes the Commission to restrict its preliminary finding of necessity to those markets or to reach a different conclusion based on market conditions today. Put another way, any contract market has a limited ability, closely linked to the market's size, to absorb the establishment and liquidation of large speculative positions in an orderly manner.[138] The silver and natural gas examples illustrate these issues, but the reasoning applies beyond their specific facts. Accordingly, the Commission preliminarily finds it necessary to implement position limits as a prophylactic measure for the 25 core referenced futures contracts.[139]

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[134] In this vein, then-Commissioner Mark Wetjen, who was an aide to Senate Majority Leader Harry Reid during the Dodd-Frank legislative process, stated at the Commission's public meeting to adopt the December 2013 proposal that to read Section 4a(a)(2)(A) to require the same antecedent necessity finding as Section 4a(a)(1) ''does not comport with my understanding of the statute's intent as informed by my experience working as a Senate aide during consideration of these provisions.'' Statement of Commissioner Mark Wetjen, Public Meeting of the Commodity Futures Trading Commission (Nov. 5, 2013), *http://www.cftc.gov/PressRoom/SpeechesTestimony/wetjenstatement110513*.

[135] December 2013 Position Limits Proposal, 78 FR at 75685.

[136] *International Swaps and Derivatives Association* v. *United States Commodity Futures Trading Commission,* 887 F. Supp. 2d 259 (D.D.C. 2012).

[137] 7 U.S.C. 6a(a)(1).

[138] Establishment of Speculative Position Limits, 46 FR 50938, 50940 (Oct. 16, 1981).

[139] The Commission's necessity finding is also supported by the consideration of costs and benefits below.

The Commission received many comments on its preliminary alternative necessity finding; the Commission summarizes and responds to significant comments below.

*a. Studies' Lack of Consensus.*[140] The Commission stated in the December 2013 Position Limits Proposal that the lack of consensus in the studies reviewed at that time warrants acting on the side of caution and implementing position limits as a prophylactic measure, ''to protect against undue price fluctuations and other burdens on commerce that in some cases have been at least in part attributable to excessive speculation.'' [141] Some commenters suggested that a lack of consensus means instead that the Commission should not implement position limits,[142] that the issue merits further study,[143] that it would be arbitrary and capricious to implement position limits,[144] and that the desire to err on the side of caution should be irrelevant to an assessment of whether position limits are necessary.[145] In short, these comments contend that the lack of consensus means position limits cannot be necessary.[146] The Commission disagrees. The lack of consensus does not provide ''objective evidence that position limits are not necessary;'' [147] rather, it suggests that they remain controversial.[148] In response to these comments, the Commission believes that Congress could not have intended by using the word ''necessary'' to restrict the Commission from determining to implement position limits unless experts unanimously agree or form a consensus they would be beneficial. Otherwise a necessity finding would be virtually impossible and, in fact, the Commission could plausibly be stymied by interested persons publishing self-interested studies. The Commission's view in this respect is supported by the text of CEA section 4a(a)(1), which states that there shall be such limits as ''the Commission finds'' are necessary.[149] Thus, while the Commission finds the studies useful, it does not cede the necessity finding to the authors.

*b. Reliance on Silver and Natural Gas Studies.*[150] The Commission stated in the December 2013 Position Limits Proposal that it ''found two studies of actual market events to be helpful and persuasive in making its preliminary alternative necessity finding,'' [151] namely, the Interagency Silver Study [152] and the PSI Report on Excessive Speculation in the Natural Gas Market.[153] Some commenters criticized the Commission's reliance on these two studies.[154] These commenters dismissed the two studies, variously, as limited, outdated,[155] dubious,[156] unpersuasive, anecdotal, and irrelevant.[157] Other commenters characterized the episodes as extreme or unique.[158] Some commenters observed that neither study recommended position limits.[159] One noted that, ''Each study focuses on activities in a *single* market during a *limited timeframe* that occurred *years ago.*'' [160] Others noted that the Commission has undertaken no independent analysis of each market, commodity, or contract affected by this rulemaking.[161] They then claim that because particular markets or commodities have unique characteristics, one cannot extrapolate from these two specific episodes to other commodities or other markets.[162] Several commenters describe the Hunt brothers silver crisis and the collapse of the natural gas speculator Amaranth as instances of market manipulation rather than excessive speculation.[163]

As discussed above, the presence of manipulative intent or activity does not preclude the existence of excessive speculation, and traders do not need manipulative intent for the accumulation of very large positions to cause the negative consequences observed in the Hunt and Amaranth incidents. These are some reasons position limits are valuable as a prophylactic measure for, in the language of CEA section 4a(a)(1), ''preventing'' burdens on interstate commerce. The Hunt brothers, who distorted the price of silver, and Amaranth, who distorted the price of natural gas, are examples that illustrate the burdens on interstate commerce of excessive speculation that occurred in the absence of position limits, and position limits would have restricted those traders' ability to cause unwarranted price movement and market volatility, and this would be so even had their motivations been innocent. Both episodes involved extraordinarily large speculative positions, which the Commission has historically associated with excessive speculation.[164] We are also given no persuasive reason to change our conclusion that extraordinarily large speculative positions could result in sudden or unreasonable fluctuations or unwarranted price changes in other physical commodity markets, just as they did in silver and natural case in the Hunt Brothers and Amaranth episodes. Although commenters describe changes in these markets over time, the characteristics that we find salient have

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[140] The Commission observed in the December 2013 Position Limits Proposal that the studies discussed therein ''overall show a lack of consensus regarding the impact of speculation on commodity markets and the effectiveness of position limits.'' 78 FR at 75695.

[141] December 2013 Position Limits Proposal, 78 FR at 75695.

[142] *E.g.,* CL–CCMR–59623 at 4–5; CL–EEI–EPSA–59602 at 3; CL–FIA–59595 at 7; and CL–IECAssn–59679 at 3.

[143] *E.g.,* CL–BG Group–59656 at 3; CL–EEI–EPSA–59602 at 3; and CL–WGC–59558 at 2.

[144] CL–Chamber–59684 at 4.

[145] CL–CCMR–59623 at 4–5.

[146] *Contra* CL–AFR–59711 at 1; CL–AFR–59685 at 1; CL–Public Citizen–59648 at 3; CL–WEED–59628.

[147] CL–EEI–EPSA–59602 at 3.

[148] A discussion of the cumulative studies reviewed by the Commission follows below. *See* below, Section I.C.2. (discussing studies and reports received or reviwed in connection with the December 2013 Position Limits Proposal), and accompanying text.

[149] This assumes that, contrary to the Commission's interpretation of the statute, Congress did not make that determination itself as to physical commodity markets.

[150] The Commission stated in the December 2013 Position Limits Proposal that it found two studies of actual market events to be helpful and persuasive in making its preliminary alternative necessity finding, namely, the interagency report on the silver crisis, U.S. Commodity Futures Trading Commission, ''Part Two, A Study of the Silver Market, May 29, 1981, Report to The Congress in Response to Section 21 of the Commodity Exchange Act, and the PSI Report on, U.S. Senate, ''Excessive Speculation in the Natural Gas Market,'' June 25, 2007.

[151] December 2013 Position Limits Proposal, 78 FR at 75695.

[152] Commodity Futures Trading Commission, Report to The Congress in Response to Section 21 of the Commodity Exchange Act, May 29, 1981, Part Two, A Study of the Silver Market.

[153] Excessive Speculation in the Natural Gas Market, Staff Report with Additional Minority Staff Views, Permanent Subcommittee on Investigations, United States Senate, Released in Conjunction with the Permanent Subcommittee on Investigations June 25 & July 9, 2007 Hearings.

[154] One commenter called the Commission's choice 'cherry-picking.' CL–Citadel–59717 at 4.

[155] The Commission disagrees; that an exemplary event occurred in the past does not make it irrelevant.

[156] *Contra* CL–Sen. Levin–59637 at 6 (pointing to ''concrete examples'').

[157] *E.g.,* CL–Chamber–59684 at 3; CL–CME–59718 at 3, 18; CL–IECAssn–59679 at 2; CL–ISDA/SIFMA–59611 at 12; and CL–USCF–59644 at 3.

[158] *E.g.,* CL–IECAssn–59679 at 2; and CL–BG Group–59656 at 3. Certainly the Commission seeks to prevent extreme events such as Amaranth and the Hunt brothers, however infrequently they may occur.

[159] *E.g.,* CL–CME–59718 at 18; and CL–CCMR–59623 at 3.

[160] CL–CME–59718 at 18.

[161] *E.g.,* CL–EEI–EPSA–59602 at 2; CL–WGC–59558 at 2.

[162] *E.g.,* CL–Citadel–59717 at 4; CL–ISDA/SIFMA–59611 at 12–14; CL–MFA–59606 at 10; and CL–WGC–59558 at 2.

[163] *E.g.,* CL–Better Markets–59716 at 12; CL–BG Group-59656 at 3; CL–COPE–59622 at 4–5; CL–CCMR–59623 at 4; CL–ISDA/SIFMA–59611 at 13; and CL–AMG–59709 at 5.

[164] December 2013 Position Limits Proposal, 78 FR at 75685, n. 60.

not changed materially.[165] Thus, these two examples remain relevant and compelling.

CME makes a textual argument in support of the position that CEA section 4a(a)(2) requires a commodity-by-commodity determination that position limits are necessary. It cites several places in CEA section 4a(a)(1) that refer to limits as necessary to eliminate ''such burden'' on ''such commodity'' or ''any commodity.'' [166] However, the prophylactic measures described herein address vulnerabilities characteristic of each market.[167] Accordingly, the Commission believes the statute's use of the singular is immaterial.[168]

The Commission's analysis applies to all physical commodities, and it would account for differences among markets by setting the limits at levels based on updated data regarding estimated deliverable supply in each of the given underlying commodities in the case of spot-month limits or based on exchange recommendation, if an exchange recommended a spot-month limit level of less than 25 percent of estimated deliverable supply, and open interest in the case of single-month and all-months-combined limits, for each separate commodity. The Commission's Reproposal regarding whether to adopt conditional spot-month limits is also based on updated data.[169] The Commission also does not find it relevant that the Interagency Silver Study and the PSI Report, each of which was published before the Dodd-Frank Act became law, do not recommend the imposition of position limits. Based on the facts described in those reports, along with the Commission's understanding of the policies underlying CEA section 4a(a)(1) in light of the Commission's own experience with legacy limits, the Commission preliminarily finds that position limits are necessary within the meaning of that section.

*c. Commission research.* One commenter asserted that the Commission failed ''to conduct proper economic analysis to determine, if in fact, the position limits as proposed were likely to have any positive impact in promoting fair and orderly commodity markets.'' [170] While acknowledging the Commission's resource constraints, this commenter remarked on ''the paucity of the published record by the CFTC's s own staff'' [171] and suggests that outside authors be given ''controlled access to all of the CFTC's data regarding investor and hedger trading records.'' [172] This commenter then proceeds to accuse the Commission of failing to ''conduct such research because they felt the data would not in fact support the proposed position limit regulations.'' [173]

The Commission disagrees that it has failed to conduct proper economic analysis to determine the likely benefits of position limits. CEA section 15(a) requires that before promulgating a regulation under the Act, the Commission consider the costs and benefits of the action according to five statutory factors. The Commission does so below in robust fashion with respect to the Reproposal in its entirety, including the alternative necessity finding. Neither section 15(a) of the CEA nor the Administrative Procedure Act requires the Commission to conduct a study in any particular form so long as it considers the costs and benefits and the entire administrative record. Section 719(a) of the Dodd-Frank Act, on the other hand, provides that the Commission ''shall conduct a study of the effects (if any) of the position limits imposed pursuant to the . . . [CEA] on excessive speculation'' and report to Congress on such matters after the imposition of position limits.[174] The Commission will do so as required by Section 719(a), thereby fully discharging its duty. At all stages, the Commission has relied on and will continue to rely on the input of staff economists in the Division of Market Oversight (''DMO'') and the Office of the Chief Economist (''OCE'').

d. Excessive Speculation

One commenter opined that, ''in discussing only the Hunt Brothers and Amaranth case studies the Commission has not given adequate weight to the benefits that speculators provide to the market.'' [175] To the contrary, the Commission recognizes that speculation is part of a well-functioning market, particularly insofar as speculators contribute valuable liquidity. The focus of this reproposed rulemaking is not speculation *per se;* Congress identified *excessive* speculation as an undue

[165] *See infra* Section I.C.1.f., and accompanying text.

[166] CL–CME–59718 at 13–14.

[167] *See, e.g.,* Establishment of Speculative Position Limits, 46 FR at 50940 (Oct. 16, 1981) (''[I]t appears that the capacity of any contract market to absorb the establishment and liquidation of large speculative positions in an orderly manner is related to the relative size of such positions, *i.e.,* the capacity of the market is not unlimited.'').

[168] *See also* 1 U.S.C. 1 (''In determining the meaning of any Act of Congress, unless the context indicates otherwise—words importing the singular include and apply to several persons, parties, or things[.]'')

[169] *See* the Commission's discussion of its verification of estimates of deliverable supply and work with open interest data, below.

[170] CL–USCF–59644 at 2.

[171] CL–USCF–59644 at 2. This commenter exaggerates. The last arguably relevant report of Commission staff is ''Commodity Swap Dealers & Index Traders with Commission Recommendations'' (Sept. 2008), available at *http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/cftcstaffreportonswapdealers09.pdf.* However, several authors or co-authors of academic papers reviewed by the Commission are or have been affiliated with the Commission in various capacities and have added to the current literature relating to position limits. Each of Harris, *see* note240, Kirilenko, *see* note 2400, and Overdahl, *see* notes 240 and 241, are former Chief Economists of the Commission. Other authors, *e.g.,* Aulerich, Boyd, Brunetti, Büyükşahin, Einloth, Haigh, Hranaiova, Kyle, Robe, and Rothenberg, are now or have been staff and/or consultants to the Commission, have spent sabbaticals at the Commission, or have been detailed to the Commission from other federal agencies. Graduate students studying with some study authors, including some working on dissertations, have also cycled through the Commission as interns. *Cf.* note 180 (disclaimer on paper by Harris and Büyükşahin).

[172] CL–USCF–59644 at 3. Data regarding investor and hedger trading records may be protected by section 8 of the CEA, 7 U.S.C. 12. In general, ''the Commission may not publish data and information that would separately disclose the business transactions or market positions of any person and trade secrets or names of customers . . . .'' 7 U.S.C. 12(a)(1). The Commission must therefore be very careful about granting outside economists access to such data. Commission registrants have in the past ''questioned why the CFTC was permitting outside economists to access CFTC data, why the CFTC was permitting the publication of academic articles using that data, and . . . the administrative process by which the CFTC was employing these outside economists.'' Review of the Commodity Futures Trading Commission's Response to Allegations Pertaining to the Office of the Chief Economist, Prepared by the Office of the Inspector General, Commodity Futures Trading Commission, Feb. 21. 2014, at ii, available at *http://www.cftc.gov/idc/groups/public/@freedomofinformationact/documents/file/oigreportredacted.pdf.* The Commission is sensitive to these concerns, and strives to ensure that reports and publications that rely on Commission data do not reveal sensitive information. To do so requires an expenditure of effort by Commission staff.

[173] CL–USCF–59644 at 3. The Commission rejects the commenter's aspersion. The Commission's Office of the Inspector General addressed the perception of institutional censorship in its ''Follow Up Report: Review of the Commodity Futures Trading Commission's Response to Allegations Pertaining to the Office of the Chief Economist, Jan. 13, 2016 (''Follow Up Report''), available at *http://www.cftc.gov/idc/groups/public/@aboutcftc/documents/file/oig_oce011316.pdf.* The Follow Up Report emphasizes ''that there has been no allegation that the Chairman or Commissioners have attempted to prevent certain topics from being researched or to alter conclusions,'' Follow Up Report at 11, but nevertheless recommended ''that OCE not prohibit research topics relevant to the CFTC mission.'' Follow Up Report at 10. The Follow Up Report observed that recently ''OCE has focused almost exclusively on short-term research and economic analysis in support of other Divisions and the Commission.'' Follow Up Report at 10.

[174] 15 U.S.C. 8307(a). *See* December 2013 Position Limits Proposal, 78 FR at 75684 (discussing section 719(a) of the Dodd-Frank Act in the context of the Commission's construal of CEA section 4a(a) to mandate that the Commission impose position limits).

[175] CL–MFA–59606 at 11–12.

burden on interstate commerce in CEA section 4a(a)(1).[176]

One commenter asserted that the Commission must provide a definition of excessive speculation before making any necessity finding.[177] The Commission disagrees that the rule must include such a definition. The statute contains no such requirement, and did not contain such a requirement prior to the Dodd-Frank Act. The Commission has never based necessity findings on a rigid definition. The Commission's position on this issue has been clear over time: ''The CEA does not define excessive speculation. But the Commission historically has associated it with extraordinarily large speculative positions . . . .'' [178] CEA section 4a(a)(1) states that position limits should diminish, eliminate, or prevent burdens on interstate commerce associated with sudden or unreasonable fluctuations or unwarranted changes in the price of commodities.[179] It stands to reason that excessive speculation involves positions large enough to risk such unreasonable fluctuations or unwarranted changes. This commenter also urges the Commission to ''demonstrate and determine that . . . harmful excessive speculation exists or is reasonably likely to occur with respect to particular commodities'' [180] before implementing any position limits.[181] As stated in the December 2013 Position Limits Proposal, the Commission referenced its prior determination in 1981 ''that, with respect to any particular market, the 'existence of historical trading data' showing excessive speculation or other burdens on that market is not 'an essential prerequisite to the establishment of a speculative limit.' '' [182] The Commission reiterates this statement and underscores that these risks are characteristic of contract markets generally. Differences among markets can be addressed, as the Commission reproposes to do here, by setting the limit levels to account for individual market characteristics. Attempting to demonstrate and determine that excessive speculation is reasonably likely to occur with respect to particular commodities before implementing position limits is impractical because historical trading data in a particular commodity is not necessarily indicative of future events in that commodity. Further, it would require the Commission to determine what may happen in a forecasted future state of the market in a particular commodity. As the Commission has often repeated, position limits are a prophylactic measure. Inherently, then, position limits are designed to address the burdens of excessive speculation well before they occur, not when the Commission somehow determines that such speculation is imminent, which the Commission (or any market actor for that matter) cannot reliably do.

e. Volatility

Commenters assert, variously, that ''the volatility of commodity markets has decreased steadily over the past decade,'' [183] that ''research found that there was a negative correlation between speculative positions and market volatility,'' [184] research shows that factors other than excessive speculation were primarily responsible for specific instances of price volatility,[185] that futures markets are associated with lower price volatility,[186] that particular types of speculators provide liquidity rather than causing price volatility,[187] that position limits will increase volatility,[188] etc. It would follow, then, according to these commenters, that because they believe there is little or no volatility (no sudden or unreasonable fluctuations or unwarranted price changes), or no volatility caused by excessive speculation, position limits cannot be necessary.

As stated above, the Commission recognizes that speculation is part of a

[176] 7 U.S.C. 6a(a)(1). One commenter suggests that the Commission base speculative position limits on ''a determination of an acceptable total level of speculation that approximates the historic ratio of hedging to investor/speculative trading.'' CL–A4A–59714 at 4. The Commission declines at this time to adopt such a ratio as basis for speculative position limits. Among other things, the Commission does not now collect reliable data distinguishing hedgers from speculators. Also, there may be levels above a historic hedging ratio that still provide liquidity rather than denoting excessive speculation. While the Commission has authority under section 4a(a)(1) of the Act to impose position limits on a group or class of traders, the only way that the Commission knows how to implement limit levels based on such a historic ratio would be to impose rationing, which the Commission declines to do at this time.

[177] CL–ISDA/SIFMA–59611 at 3, 14–15; *see also* CL–FIA–59595 at 6–7.

[178] December 2013 Position Limits Proposal, 78 FR at 75685, n. 60 (citation omitted).

[179] 7 U.S.C. 6a(a)(1).

[180] CL–ISDA/SIFMA–59611 at 3; *see also* CL–CCMR–59623 at 4; CL-Chamber-59684 at 4. *Contra* CL-Sen. Levin-59637 at 6 (stating ''[c]ontrary to the complaints of some critics, it would be a waste of time and resources for the Commission to expand the proposed rules beyond the existing justification to repeat the same analysis, reach the same conclusions, and issue the same findings for each of the 28 commodities.'').

[181] *See also* CL–CCMR–59623 at 4–5. Another commenter ''contends that the best available evidence discounts the theory that there is excessive speculation distorting the prices in the commodity markets.'' CL–MFA–59606 at 13 (citing Pirrong). Such a contention is inconsistent with ''Congress' determination, codified in CEA section 4a(a)(1), that position limits are an effective tool to address excessive speculation as a cause of sudden or unreasonable fluctuations or unwarranted changes in the price of . . . [agricultural and exempt] commodities. December 2013 Position Limits Proposal, 78 FR at 75695 (footnote omitted). Another commenter mischaracterizes the finding of the Congressional Budget Report, ''Evaluating Limits on Participation and Transactions in Markets for Emissions Allowances'' (2010), available at *http://www.cbo.gov/publication/21967* (''CBO Report''); the CBO Report does not conclude ''that position limits are harmful to markets.'' CL–IECAssn–59679 at 3. Rather, in the context of creating markets for emissions allowance trading, the CBO Report discusses both the uses and benefits and the challenges and drawbacks of not only position limits but also circuit breakers, in addition to banning certain types of traders and banning allowance derivatives. Among other things, the CBO Report states, ''Position Limits would probably lessen the possibility of systemic risk and manipulation in allowance markets . . . .'' CBO Report at viii. Another commenter states that a ''CFTC study'' found that the 2008 crude oil crisis was primarily due to fundamental factors in the supply and demand of oil. CL–CCMR–59623 at 4. The referenced study is Harris and Büyükşahin, The Role of Speculators in the Crude Oil Futures Market (working paper 2009). *See generally* note 240 (listing studies that employ the Granger method of statistical analysis). While Harris is a former Chief Economist, and Büyükşahin is a former staff economist in OCE, as noted above, the cover page of the referenced paper contains the standard disclaimer, ''This paper reflects the opinions of its authors only, and not those of the U.S. Commodity Futures Trading Commission, the Commissioners, or other staff of the Commission.'' That is, it is not a ''CFTC study.'' In addition, other studies of that market at that time reached different conclusions. *Cf.* note 252 (citing study that concludes price changes precede the position change). The Commission reviewed several studies of the crude oil market around 2008 and discusses them herein. *See* discussion of persuasive academic studies, below. The Commission cautions that, given the continuing controversy surrounding position limits, it is unlikely that one study will ever be completely dispositive of these complicated and difficult issues.

[182] December 2013 Position Limits Proposal, 78 FR at 75683.

[183] CL–CCMR–59623 at 4 (claim supported only by a reference to a comment letter that pre-dates the December 2013 Position Limits Proposal).

[184] CL–MFA–59606 at 12 (citing one academic paper, Irwin and Sanders, The Impact of Index and Swap Funds on Commodity Futures Markets: Preliminary Results (working paper 2010)). *See generally note 240 (*studies that employ the Granger method of statistical analysis).

[185] *E.g.,* CL–MFA–59606 at 11–12, n. 26. *Contra* CL–AFR–59685 at 1 (stating ''We understand that other factors contribute to highly volatile commodity prices, but excessive speculation plays a significant part, according to studies by Princeton, MIT, the Petersen Institute, the University of London, and the U.S. Senate, among other highly credible sources.'').

[186] CL–MFA–59606 at 13, n. 30.

[187] E.g., CL–MFA–59606 at 12–13 (hedge funds). *Cf.* CL–SIFMA AMG–59709 at 15 (asserting ''neither Amaranth nor the Hunt brothers were in any way involved in commodity index swaps''), 16 (registered investment companies and ERISA accounts).

[188] CL–MFA- 59606 at 13. *Contra* CL–CMOC–59702 at 2 (maintaining that witness testimony before policymakers ''confirmed that the erosion of the position limits regime was a leading cause in market instability and wild price swings seen in recent years and that it had led to diminished confidence in the commodity derivative markets as a hedging and price discovery tool'').

well-functioning market particularly, as noted in comments, as a source of liquidity. Position limits address excessive speculation, not speculation *per se.* Position limits neither exclude particular types of speculators nor prohibit speculative transactions; they constrain only speculators with excessively large positions in order to diminish, eliminate, or prevent an undue and unnecessary burden on interstate commerce in a commodity.[189] The Commission agrees that futures markets are associated with, and may indeed contribute to, lower volatility in underlying commodity prices. However, as Congress observed, in CEA section 4a(a)(1), excessive speculation in a commodity contract that causes sudden or unreasonable fluctuations or unwarranted changes in the price of such commodity, is an undue and unnecessary burden on interstate commerce in such commodity.[190] In promulgating CEA section 4a(a)(1), Congress adopted position limits as a useful tool to diminish, eliminate, or prevent those problems. The Commission believes that position limits are a necessary prophylactic measure to guard against disruptions arising from excessive speculation, and the Commission has endeavored to repropose limit levels that are not so low as to hamper healthy speculation as a source of liquidity.[191]

f. Basis for Determination

One commenter states, ''The necessity finding . . . proffered by the Commission—which consists of a discussion of two historical events and a cursory review of existing studies and reports on position limits related issues—falls short of a comprehensive analysis and justification for the proposed position limits.[192] We disagree with the commenter's opinion that the Commission's analysis is not comprehensive or falls short of justifying the reproposed rule.[193]

Another commenter states that the December 2013 Position Limits Proposal ''does not provide any quantitative analysis of how the outcome of these [two historical] events might have differed if the proposed position limits had been in place.'' [194] The Commission disagrees. The Commission stated in the December 2013 Position Limits Proposal that, ''The Commission believes that if Federal speculative position limits had been in effect that correspond to the . . . . [proposed] limits . . . , across markets now subject to Commission jurisdiction, such limits would have prevented the Hunt brothers and their cohorts from accumulating such large futures positions.'' [195] This statement was based on calculations using a methodology similar to [196] that proposed in the December 2013 Position Limits Proposal applied to quantitative data included and as described therein.[197] The Commission's stated belief is unchanged at the higher single-month and all-months-combined limit levels of 7,600 contracts that the Commission adopts today for silver.[198] Nevertheless, historical data regarding absolute position size from the period of the late-1970's to 1980 may not be readily comparable to the numerical limits adopted in the current market environment. Accordingly, the Commission is reproposing establishing levels using the methodology based on the size of the current market as described elsewhere in this release.

With respect to Amaranth, the Commission stated, ''Based on certain assumptions . . . , the Commission believes that if Federal speculative position limits had been in effect that correspond to the limits that the Commission . . . [proposed in the December 2013 Position Limits Proposal], across markets now subject to Commission jurisdiction, such limits would have prevented Amaranth from accumulating such large futures positions and thereby restrict its ability to cause unwarranted price effects.'' [199] This statement of belief about Amaranth was also based on calculations using the methodology applied to quantitative data as described and included in the December 2013 Position Limits Proposal preamble.[200] The historical size of Amaranth positions would no longer breach the higher single-month and all-months-combined limit levels of 200,900 contracts that the Commission adopts today for natural gas.[201] However, the Commission is reproposing setting a level using a methodology that adapts to changes in the market for natural gas, *i.e.,* the fact that it has grown larger and more liquid since the collapse of Amaranth. Thus, it stands to reason that a speculator might now have to accumulate a larger position than Amaranth's historical position to present a similar risk of disruption to the natural gas market. In fact, the Commission has long recognized ''that the capacity of any contract market to absorb the establishment and liquidation of large speculative positions in an orderly manner is related to the relative size of such positions, *i.e.,* the capacity of the market is not unlimited.'' [202] A larger market should have larger capacity, other things being equal; [203] hence, the Commission is adopting higher levels of limits. Moreover, costly disruptions like those associated with Amaranth remain entirely possible. Because the costs of these disruptions can be great, and borne by members of the public

[189] That a particular type of speculator trades a different type of instrument, employs a different trading strategy, or is unlevered, diversified, subject to other regulatory regimes, etc., so as to distinguish it in some way from Amaranth or the Hunt brothers does not overcome the size of the position held by the speculator, and the risks inherent in amassing extraordinarily large speculative positions.

[190] CEA section 4a(a)(1); 7 U.S.C. 6a(a)(1).

[191] *See* the discussion of the impact analysis, below under § 150.2.

[192] CL–Citadel–59717 at 3–4 (footnote omitted). *Contra* CL-Sen. Levin-59637 at 6 (declaring that ''[t]he Commission's analysis and findings, paired with concrete examples, provide a comprehensive explanation of the principles and reasoning behind establishing position limits.'').

[193] Although the events described in the proposal are sufficient to support the necessity finding for the reasons given, the Commission also notes reports that more recent market events have been perceived as involving excessively large positions that have caused or threatened to cause market disruptions. *See, e.g.,* Ed Ballard, Speculators sit on Sugar Pile, Raising Fears of Selloff, The Wall Street Journal (Nov. 21, 2016) (''Speculative investors have built a record position in sugar this year, sparking fears of a swift pullback in its price.''); Of mice and markets, A surge in speculation is making commodity markets more volatile, The Economist (Sept. 10, 2016) (discussing ''scramble by funds to unwind their short positions in'' West Texas Intermediate that appears to have ''fanned a rally in spot oil prices''). As discussed elsewhere, willingness to participate in the futures and swaps markets may be reduced by perceptions that a participant with an unusually large speculative position could exert unreasonable market power.

[194] CL–WGC–59558 at 2; *see also* CL–BG Group-59656 at 3.

[195] December 2013 Position Limits Proposal, 78 FR at 75690.

[196] The Commission's methodology is a fair approximation of how the limits would have been applied during the time of the silver crisis. *See* December 2013 Position Limits Proposal, 78 FR at 75690.

[197] December 2013 Position Limits Proposal, 78 FR at 75690–1.

[198] For example, using historical month-end open interest data, the Commission calculated a single- and all-months-combined limit level of 6,700 contracts, which would have been exceeded by a total Hunt position of over 12,000 contracts for March delivery. December 2013 Position Limits Proposal, 78 FR at 75690. Baldly, a position of 12,000 contracts would still exceed a 7,600 contract limit.

[199] December 2013 Position Limits Proposal, 78 FR at 75692.

[200] December 2013 Position Limits Proposal, 78 FR at 75692–3.

[201] *See* level of initial limits under App. D to part 150.

[202] Establishment of Speculative Position Limits, 46 FR 50938, 50940.

[203] A gross comparison such as this may not meaningful. For example, the Commission could have increased the size of Amaranth's historical position proportionately to the increased size of the market and compared it to the limit level for natural gas that the Commission adopts today. But such an approach would be less rigorous than the analysis on which the Commission bases its determination today.

unconnected with trading markets, the Commission preliminarily finds it necessary to impose speculative position limits as a preventative measure. As markets differ in size, the limit levels differ accordingly, each designed to prevent the accumulation of positions that are extraordinary in size in the context of each market.

Several commenters opined that the Commission, in reaching its preliminary alternative necessity finding, ignores current market developments and does not employ the ''new tools'' other than position limits available to it to prevent excessive speculation or manipulative or potentially manipulative behavior.[204] Specifically, some commenters suggested that position limits are not necessary because position accountability rules and exchange-set limits are adequate.[205] The Commission agrees that the Dodd-Frank Act gave the Commission new tools with which to protect and oversee the commodity markets, and agrees that these along with older tools may be useful in addressing market volatility. However, the Commission disagrees that the availability of other tools means that position limits are not necessary.[206] Rather the statute, at a minimum, reflects Congress' judgment that position limits may be found by the Commission to be necessary. The Commission notes that although CEA section 4a(a) position limits provisions have existed for many years, the Dodd-Frank Act not only retained CEA section 4a(a), but added, rather than deleted, several sections. This leads to the conclusion that Congress appears to share the Commission's view that the other tools provided by Congress were not sufficient.

Position accountability, for example, is an older tool, from the era of the CFMA. As the Commission explained in the December 2013 Position Limits Proposal, the CFMA ''provided a statutory basis for exchanges to use pre-existing position accountability levels as an alternative means to limit the burdens of excessive speculative positions. Nevertheless, the CFMA did not weaken the Commission's authority in CEA section 4a to establish position limits as an alternative means to prevent such undue burdens on interstate commerce. More recently, in the CFTC Reauthorization Act of 2008, Congress gave the Commission expanded authority to set position limits for significant price discovery contracts on exempt commercial markets,'' [207] and it expanded the Commission's authority again in the Dodd-Frank Act.[208] While position accountability is useful in providing exchanges with information about specific trading activity so that exchanges can act if prudent to require a trader to reduce a position after the position has already been amassed, position limits operate prophylactically without requiring case-by-case, ex post determinations about large positions. As to exchange-set accountability levels or position limits set at levels below those of federal position limits, those remain useful as well and should be used, at the exchanges' discretion, in conjunction with federal position limits. They may be most useful, for example, with respect to contracts that are not core-referenced futures contracts or if an exchange determines that federal limits are too high to address adequately the conditions in the markets it administers. In the regulations that the Commission reproposes today, the Commission would update (rather than eliminate) the acceptable practices for exchange-set speculative position limits and position accountability rules to conform to the Dodd-Frank Act changes [as described in the December 2013 Position Limits Proposal].[209] Generally, for contracts subject to speculative limits, exchanges may set limits no higher than the federal limits,[210] and may impose ''restrictions . . . to reduce the threat of market manipulation or congestion, to maintain orderly execution of transactions, or for such other purposes consistent with its responsibilities.'' [211] And § 150.5(b)(3) sets forth the requirements for position accountability in lieu of exchange-set limits in the case of contracts not subject to federal limits. The exchanges are also still authorized to react to instances of greater price volatility by exercising emergency authority as they did during the silver crisis.[212] In addition, the Commission has striven to take current market developments into account by considering the market data to which the Commission has access as described herein and by considering the description of current market developments to the extent included in the comments the Commission has received in connection with the December 2013 Position Limits Proposal. Some commenters suggest that the Commission, in reaching its preliminary alternative necessity finding, has not undertaken any empirical analysis of available data.[213] As discussed above, the Commission carefully reviewed the Interagency Silver Study and the PSI Report on Excessive Speculation in the Natural Gas Market.[214] The Commission also carefully considered the studies submitted during the various comment periods regarding the December 2013 Position Limits Proposal and the 2016 Supplemental Position Limits Proposal. Other commenters suggest that the Commission relies on incomplete, unreliable, or out of date data, and that the Commission should collect more and/or better data before determining that position limits are necessary or implementing position limits.[215] The Commission disagrees. The Commission has considered the recent data presented by the exchanges in support of their estimates of deliverable supply. The Commission is expending significant, agency-wide efforts to improve data collection and to analyze the data it receives. The quality of the data on which the Commission relies has improved since the December 2013 Position Limits Proposal. The Commission is satisfied with the quality of the data on which it bases its Reproposal.

One commenter opines that, ''The Proposal's 'necessary' finding offers no reasoned basis for adopting its framework and the shift in regulatory policy it embodies.'' [216] To the contrary,

[204] *E.g.,* CL–CCMR–59623 at 3 (supporting additional transparency and reporting); CL-Citadel–59717 at 4 (pointing to available tools, including ''enhanced market surveillance, broadened reporting requirements, broadened special call authorities, and exchange limits''); CL–ISDA/SIFMA–59611 at 13 (noting that tools that the Commission has incorporated include ''enhanced market surveillance, broadened reporting requirements, broadened special call authorities, and exchange limits''); CL–MFA–59606 at 10; and CL–SIFMA AMG–59709 at 5–6 (providing examples of new tools).

[205] *E.g.,* CL–CME–59718 at 18; CL–ICE–59645 at 2–4; CL–FIA–59595 at 6, n. 13, 12–13; and CL–AMG–59709 at 8.

[206] The Commission observes that logically there is no reason why the availability of some regulatory tools under the CEA should preclude the use of another tool explicitly authorized by Congress.

[207] 78 FR at 75681 (footnotes omitted).

[208] *See generally* December 2013 Position Limits Proposal, 78 FR at 75681.

[209] *See generally* December 2013 Position Limits Proposal, 78 FR at 75747–8.

[210] *See* discussion of requirements for exchange-set position limits under § 150.5, below, and exchange core principles regarding position limits, below.

[211] *See* reproposed § 150.5(a)(6)(iii).

[212] *See generally* 7 U.S.C. 7(d)(6) (DCM Core Principles: Emergency Authority); 7 U.S.C. 7b–3(f)(8) (Core Principles for Swap Execution Facilities—Emergency Authority); 17 CFR 37.800 (Swap Execution Facility Core Principle 8—Emergency authority), 17 CFR 38.350 (Designated Contract Markets –Emergency Authority—Core Principle 6).

[213] *E.g.,* CL–FIA–59595 at 3; CL–EEI–EPSA–59602 at 2, 8–9.

[214] *See supra* Section I.C.2 (discussing the Interagency Silver Study and the PSI Report on Excessive Speculation in the Natural Gas Market).

[215] *E.g.,* CL-Citadel-59717 at 4–5; CL–EEI–EPSA–59602 at 8–9.

[216] CL–CME–59718 at 3.

the necessity finding, including the Commission's responses to comments, is the Commission's explanation of why position limits are necessary.[217]

g. Non-Spot-Month Limits

Some commenters opine that ''the Commission's proposed non-spot-month position limits do not increase the likelihood of preventing the excessive speculation or manipulative trading exemplified by Amaranth or the Hunt brothers relative to the status quo.'' [218] The Commission disagrees; as repeated above, ''the capacity of the market is not unlimited.'' [219] This includes markets in non-spot month contracts. Thus, as with spot-month contracts, extraordinarily large positions in non-spot month contracts may still be capable of distorting prices.[220] If prices are distorted, the utility of hedging may decline.[221] One commenter argues for non-spot month position accountability rules; [222] the Commission discusses position accountability above.[223] Another argues that Amaranth was really just ''another case of spot-month misconduct.'' [224] The Commission disagrees that this limits the relevance of Amaranth; a speculator like Amaranth may attempt to distort the perception of supply and demand in order to benefit, for instance, calendar spread positions by, for instance, creating the perception of a nearby shortage of the commodity which a speculator could do by accumulating extraordinarily large long positions in the nearby month.[225] One commenter states that ''improperly calibrated non-spot month limits would also deter speculative activity that triggers no risk of manipulation or 'causing sudden or unreasonable fluctuations or unwarranted changes in the price of such commodity,' the hallmarks of 'excessive speculation.' '' [226] The Commission sees little merit in this objection because the Reproposal would calibrate the levels of the non-spot month limits to accommodate speculative activity that provides liquidity for hedgers.

h. Meaning of Necessity

One commenter suggests that position limits could only be necessary if they were the only means of preventing the Hunt brothers and Amaranth crises.[227] First, while the Commission relies on these incidents to explain its reasoning, the risks they illustrate apply to all markets in physical commodities, and so the efficacy of the limits the Commission adopts today, and the extent to which other tools are sufficient, cannot be judged solely by whether they might have prevented those specific incidents. Second, in any event, the Commission rejects such an overly restrictive reading, which lacks a basis in both common usage and statutory construction. The Commission preliminarily finds that limits are necessary as a prophylactic tool to strengthen the regulatory framework to prevent excessive speculation *ex ante* to diminish the risk of the economic harm it may cause further than it would reliably be from the other tools alone. Other commenters question why the Commission proposed limits at levels they contend are too high to be effective, undercutting the Commission's alternative necessity finding.[228] One commenter points out that the limit levels as proposed would not have prevented the misconduct alleged by the Commission in a particular enforcement action filed in 2011.[229] As repeated elsewhere in this Notice [230] and in the December 2013 Position Limits Proposal,[231] in establishing limits, the Commission must, ''to the maximum extent practicable, in its discretion . . . ensure sufficient market liquidity for bona fide hedgers.[232] The Commission realizes that the reproposed initial limit levels may prevent or deter some, but fail to eliminate all, excessive speculation in the markets for the 25 commodities covered by this first phase of implementation. But the Commission is concerned that initial limit levels set lower than those reproposed today, and in particular low enough to prevent market manipulation or excessive speculation in specific, less egregious cases than the Hunt brothers or Amaranth, could impair liquidity for hedges.[233]

The Commission requests comment on all aspects of this section.

2. Studies and Reports

The Commission has reviewed and evaluated studies and reports received as comments on the December 2013 Position Limits Proposal, in addition to the studies and reports reviewed in connection with the December 2013 Position Limits Proposal [234] (such

[217] *See* CL–Sen. Levin–59637 at 6 (stating that the Commission's necessity finding ''appropriately reflects Congressional action in enacting the Dodd-Frank Act which requires the Commission to impose appropriate position limits on speculators trading physical commodities.'').

[218] CL–AMG–59709 at 9. *See* the Commission's response to the comment regarding the purported lack of ''quantitative analysis of how the outcome of these [two historical] events might of differed if the proposed position limits had been in place'' at the text accompanying notes 192–200 above. *See also* CL–CME–59718 at 41–3; CL–ISDA/SIFMA–59611 at 28.

[219] *See* note 202 *supra* and accompanying text.

[220] *See* December 2013 Position Limits Proposal, 78 FR at 75691 (citing the PSI Report, ''Amaranth accumulated such large positions and traded such large volumes of natural gas futures that it distorted market prices, widened price spread, and increased price volatility.'').

[221] *See* December 2013 Position Limits Proposal, 78 FR at 75692 (citing the PSI Report, ''Commercial participants in the 2006 natural gas markets were reluctant or unable to hedge.'').

[222] CL–CME–59718 at 41–42.

[223] *See* notes 207–212 *supra* and accompanying text.

[224] CL–ISDA/SIFMA–59611 at 28.

[225] The Commission discussed the trading activity of Amaranth at length in the December 2013 Position Limits Proposal, 78 FR at 75691–3; in particular, Amaranth's calendar spread trading is discussed at 78 FR 75692. The Commission repeats that the findings of the Permanent Subcommittee in the PSI Report support the imposition of speculative position limits outside the spot month. A trader, who does not liquidate an extraordinarily large long futures position in the nearby physical-delivery futures contract, contrary to typical declining open interest patterns in a physical-delivery contract approaching expiration, may cause the nearby futures price to increase as short position holders, who do not wish to make physical delivery, bid up the futures price in an attempt to offset their short positions. Potential liquidity providers who do not currently hold a deliverable commodity may be hesitant to establish short positions as a physical-delivery futures contract approaches expiration, because exchange rules and contract terms require such short position holder to prepare to make delivery by obtaining the cash commodity.

[226] CL–CME–59718 at 43; *cf.* CL–APGA–59722 at 3 (asserting that ''the non-spot month limits being proposed by the Commission are too high to be effective'').

[227] CL–CCMR–59623 at 4.

[228] CL–ISDA/SIFMA–59611 at 28; CL–Better Markets–59716 at 24; CL–APGA–59722 at 6–7.

[229] CL–Better Markets–59716 at 22, n. 38 (Parnon Energy).

[230] *See* the discussion in levels of limits, under § 150.2, below.

[231] *E.g.,* December 2013 Position Limits Proposal, 78 FR at 75681.

[232] CEA section 4a(a)(3)(B)(iii), 7 U.S.C. 6a(a)(3)(B)(iii). Some commenters expressed concern that position limits could disproportionately affect commercial entities. *E.g.,* CL–CME–59718 at 43; CL–APGA–59722 at 3. Some commenters expressed concern about the application of position limits to trade options. *E.g.,* CL–APGA–59722 at 3; CL–EEI–EPSA–59602 at 3. The Commission reminds commenters that speculative position limits do not apply to bona fide hedging transactions or positions. CEA section 4a(c), 7 U.S.C. 6a(c).

[233] The Commission will revisit the specific limitations set forth in CEA section 4a(a)(3) when, under reproposed § 150.2(e), it considers resetting limit levels.

[234] A list of studies and reports that the Commission reviewed in connection with the December 2013 Position Limits Proposal was included in its Appendix A to the preamble. December 2013 Position Limits Proposal, 78 FR at 75784–7. One commenter observed that the studies reviewed in connection with the December 2013 Position Limits Proposal are not all ''necessarily germane to specific position limits proposed.'' CL–Citadel–59717 at 4. *See also* CL–CCMR–59623 at 5 (stating that it had reviewed the studies, and found that ''only 27 address position limits''). The Commission acknowledges that some studies are more relevant than others. The Commission in the December 2013 Position Limits Proposal was disclosing the studies that it had reviewed and

studies and reports, collectively, ''studies''). Appendix A to this preamble is a summary of the various studies reviewed and evaluated by the Commission.

The Commission observed in the December 2013 Position Limits Proposal, ''There is a demonstrable lack of consensus in the studies.'' [235] Neither the passage of time nor the additional studies have changed the Commission's view: As a group, these studies do not show a consensus in favor of or against position limits.[236] In addition to arriving at disparate conclusions, the quality of the studies varies. Nevertheless, the Commission believes that some well-executed studies suggest that excessive speculation cannot be excluded as a possible cause of undue price fluctuations and other burdens on commerce in certain circumstances. All of these factors persuade the Commission to act on the side of caution in preliminarily finding limits necessary, consistent with their prophylactic purpose. For these reasons, explained in more detail below, the Commission preliminarily concludes that the studies, individually or taken as a whole, do not persuade the Commission to reverse course [237] or to change its necessity finding.[238]

The Commission's deliberations are informed by its consideration of the studies. The Commission recognizes that speculation and volatility are not *per se* unusual or exceptional occurrences in commodity markets. Some economic studies attempt to distinguish normal, helpful speculative activity in commodity markets from excessive speculation, and normal volatility from unreasonable price fluctuations. It has proven difficult in some studies to discriminate between the proper workings of a well-functioning market and unwanted phenomena. That some studies have as yet failed to do so with precision or certainty does not, in light of the full record, persuade the Commission to reverse course or to change its necessity finding.

In general, many studies focused on subsidiary questions and did not directly address the desirability or utility of position limits. Their proffered interpretations may not be the only plausible explanation for statistical results. There is no broad academic consensus on the formal, testable economic definition of ''excessive speculation'' in commodity futures markets or other relevant terms such as ''price bubble.'' There is also no broad academic consensus on the best statistical model to test for the existence of excessive speculation. There are not many papers that quantify the impact and effectiveness of position limits in commodity futures markets. The Commission has identified some reasons why there are not many compelling, peer-reviewed economic studies engaging in quantitative, empirical analysis of the impact of position limits on prices or price volatility: Limitations on publicly available data, including detailed information on specific trades and traders; pre-existing position limits in some commodity markets, making it difficult to determine how those markets would operate in the absence of position limits; and the difficulties inherent in modelling complex economic phenomena.

The studies that the Commission considered can be grouped into seven categories.[239]

Granger Causality Analyses [240]

evaluated. The Commission requested comment on its discussion of the studies, and invited commenters to advise the Commission of other studies to consider, in the hope that commenters would indicate which studies they believe are more germane or persuasive and suggest other studies for Commission review.

[235] December 2013 Position Limits Proposal, 78 FR at 75694.

[236] *See* 162 Cong. Rec. E1005–03, E1006 (June 28, 2016) (Statement of Rep. Conaway, Chairman of the House Committee on Agriculture) (''Comment letters on either side declaring that the matter is settled in their favor among respectable economists are simply incorrect.''). *Contra* CL–CCMR–59623 at 5, which says, ''The Committee staff also reviewed these studies and found that of them, only 27 address position limits, with the majority opposing such limits.'' The commenter describes how it arrives at this conclusion as follows: ''The Committee staff reviewed the abstract and body of each study to determine if the author assessed: (1) Whether position limits are effective at reducing speculation; or (2) whether excessive speculation is distorting prices in commodities markets. If the author presented a critical analysis of the issue, rather than just mentioning position limits or excessive speculation in passing, then the Committee staff included the study in its tally.'' Such a method is relatively unsophisticated, and the Commission cannot evaluate it without knowing to which studies the commenter refers. The commenter continues, ''Of the total, 105 studies address whether excessive speculation is distorting prices in today's commodity markets, with 66 of these studies finding that excessive speculation is not a problem.'' This statement did not identify the 66 studies or 105 studies on which it based its belief. Accordingly, the Commission is unable to evaluate the basis of its belief.

[237] *See* discussion of mandate, above. We emphasize that this discussion relates only to the Commission's alternative necessity finding. To the extent there is a Congressional mandate that the Commission establish position limits, these studies could be no basis to disregard it. As noted in the December 2013 Position Limits Proposal, ''Studies that militate against imposing any speculative position limits appear to conflict with the Congressional mandate . . . that the Commission impose limits on futures contracts, options, and certain swaps for agricultural and exempt commodities.'' 78 FR at 75695 (footnote omitted). Separately, ''such studies also appear to conflict with Congress' determination, codified in CEA section 4a(a)(1), that position limits are an effective tool to address excessive speculation as a cause of sudden or unreasonable fluctuations or unwarranted changes in the price of such commodities,'' irrespective of whether they are mandated. *Id.* The Commission acknowledges that some of the studies, when considered as comments on the December 2013 Position Limits Proposal, can be understood to suggest that, contrary to the Congressional determination, there is no empirical evidence that excessive speculation exists, that excessive speculation causes sudden or unreasonable fluctuations or unwarranted changes in the price of a commodity, or is an undue and unnecessary burden on interstate commerce in a commodity.

[238] *See* discussion of necessity finding, above.

[239] These categories are not exclusive; some studies employ or examine more than one type of methodology. That researchers in the different categories employed different methodologies complicates the task of comparing the studies across the seven categories. In addition, some studies were not susceptible to meaningful economic analysis for various reasons, such as being written in a foreign language, being founded on suspect methodologies, being press releases, etc. These studies include: Basak and Pavlova, A Model Financialization of Commodities (working paper 2013); Bass, Finanazmärkte als Hungerverursacher? (working paper 2011); Bass, Finanzspekulation und Nahrungsmittelpreise. Anmerkungenzum Stand der Forschung (working paper 2013); Bukold, Ölpreisspekulation und Benzinpreise in Deutschland, (2011); Chevalier, (Ministère de l'Economie, de l'Industrie e t de l'emploi): Rappor t du groupe de travai l sur la volatilitè des prix du pètrole, (2010); Dicker, Oil's Endless Bid, (2011); Ederington and Lee, Who Trades Futures and How: Evidence from the Heating Oil Market?, Journal of Business 2002; Evans, The Official Demise of the Oil Bubble, Wall Street Journal 2008; Gheit and Katzenberg, Surviving Lower Oil Prices, Oppenheimer & Co. (2008); Ghosh, Commodity Speculation and the Food Crisis, (working paper 2010); Halova, The Intraday Volatility-Volume Relationship in Oil and Gas Futures, (working paper 2012); Jouyet, Rappor t d' étape-Prévenir e t gérer l'instabilité des marchés agricoles, (2010); Korzenik, Fundamental Misconceptions in the Speculation Debate, (2009); Lake Hill Capital Management, Investable Indices are Distorting Commodity Markets?, (2013); Lee, Cheng, and Koh, Would Position Limits Have Made any Difference to the 'Flash Crash' on May 6, 2010?, Review of Futures Markets (2010); Markham, Manipulation of Commodity Futures Prices: The Unprosecutable Crime, Yale Journal of Regulation (1991); Mayer, The Growing Financializsation of Commodity Markets: Divergences between Index Investors and Money Managers, Journal of Development Studies (2012); Morse, Oil dotcom, Research Notes, (2008); Naylor, Food Security in an Era of Economic Volatility (working paper 2010); Newell, Commodity Speculation's ''Smoking Gun'' (2008); Peri, Vandone, and Baldi, Internet, Noise Trading and Commodity Prices (working paper 2012); Soros, Interview with Stern Stern Magazine (2008); Tanaka, IEA Says Speculation Amplifying Oil Price Moves, (2006); Von Braun and Tadesse, Global Food Price Volatility and Spikes: An Overview of Costs, Cause and Solutions (2012).

[240] Studies that employ the Granger method of statistical analysis include: Algieri, Price Volatility,

Continued

Some economic studies considered by the Commission employ the Granger method of statistical analysis. The Granger method seeks to assess whether there is a strong linear correlation between two sets of data that are arranged chronologically forming a ''time series.'' While the Granger test is referred to as the ''Granger causality test,'' it is important to understand that, notwithstanding this shorthand, ''Granger causality'' does not necessarily establish an actual cause and effect relationship. The result of the Granger method is evidence, or the lack of evidence, of the existence of a linear correlation between the two time series. The absence of Granger causality does not necessarily imply the absence of actual causation.

Comovement or Cointegration Analyses [241]

The comovement method looks for whether there is correlation that is contemporaneous and not lagged. A subset of these comovement studies use a technique called cointegration for testing correlation between two sets of data.

Models of Fundamental Supply and Demand [242]

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Speculation and Excessive Speculation in Commodity Markets: Sheep or Shepherd Behaviour? (working paper 2012); Antoshin, Canetti, and Miyajima, IMF Global Financial Stability Report: Financial Stress and Deleveraging: Macrofinancial Implications and Policy, Annex 1.2, Financial Investment in Commodities Markets (October 2008); Aulerich, Irwin, and Garcia, Bubbles, Food Prices, and Speculation: Evidence from the CFTC's Daily Large Trader Data Files (NBER Conference 2012); Borin and Di Nino, The Role of Financial Investments in Agricultural Commodity Derivatives Markets (working paper 2012); Brunetti and Büyükşahin, Is Speculation Destabilizing? (working paper 2009); Cooke and Robles, Recent Food Prices Movements: A Time Series Analysis (working paper 2009); Frenk, Review of Irwin and Sanders 2010 OECD Report (Better Markets June 10, 2010); Gilbert, Commodity Speculation and Commodity Investment (2010); Gilbert, How to Understand High Food Prices, Journal of Agricultural Economics (2008); Gilbert, Speculative Influences on Commodity Futures Prices, 2006–2008, UN Conference on Trade and Development (2010); Goyal and Tripathi, Regulation and Price Discovery: Oil Spot and Futures Markets (working paper 2012); Grosche, Limitations of Granger Causality Analysis to Assess the Price Effects From the Financialization of Agricultural Commodity Markets Under Bounded Rationality, Agricultural and Resource Economics (2012); Harris and Büyükşahin, The Role of Speculators in the Crude Oil Futures Market (working paper 2009); Irwin and Sanders, Energy Futures Prices and Commodity Index Investment: New Evidence from Firm-Level Position Data (working paper 2014); Irwin and Sanders, The Impact of Index and Swap Funds on Commodity Futures Markets: A Systems Approach, Journal of Alternative Investments (working paper 2010); Irwin and Sanders, The Impact of Index and Swap Funds on Commodity Futures Markets: Preliminary Results (working paper 2010); Irwin and Sanders, The ''Necessity'' of New Position Limits in Agricultural Futures Markets: The Verdict from Daily Firm-Level Position Data (working paper 2014); Irwin and Sanders, The Performance of CBOT Corn, Soybean, and Wheat Futures Contracts after Recent Changes in Speculative Limits (working paper 2007); Irwin, Sanders, and Merrin, Devil or Angel: The Role of Speculation in the Recent Commodity Price Boom, Journal of Agricultural and Applied Economics (2009); Kaufman, The role of market fundamentals and speculation in recent price changes for crude oil, Energy Policy, Vol. 39, Issue 1 (January 2011); Kaufmann and Ullman, Oil Prices, Speculation, and Fundamentals: Interpreting Causal Relations Among Spot and Futures Prices, Energy Economics, Vol. 31, Issue 4 (July 2009); Mayer, The Growing Interdependence Between Financial and Commodity Markets, UN Conference on Trade and Development (discussion paper 2009); Mobert, Do Speculators Drive Crude Oil Prices? (2009 working paper); Robles, Torero, and von Braun, When Speculation Matters (working paper 2009); Sanders, Boris, and Manfredo, Hedgers, Funds, and Small Speculators in the Energy Futures Markets: An Analysis of the CFTC's Commitment of Traders Reports, Energy Economics (2004)*;* Sanders, Irwin, and Merrin, The Adequacy of Speculation in Agricultural Futures Markets: Too Much of a Good Thing?, Applied Economic Perspectives and Policy (2010); Sanders, Irwin, and Merrin, Smart Money? The Forecasting Ability of CFTC Large Traders, Journal of Agricultural and Resource Economics (2009); Sanders, Irwin, and Merrin, A Speculative Bubble in Commodity Futures? Cross-Sectional Evidence, Agricultural Economics (2010); Singleton, The 2008 Boom/Bust in Oil Prices (working paper 2010); Singleton, Investor Flows and the 2008 Boom/Bust in Oil Prices (working paper 2011); Stoll and Whaley, Commodity Index Investing and Commodity Futures Prices (working paper 2010); Timmer, Did Speculation Affect World Rice Prices?, UN Food and Agricultural Organization (working paper 2009); Tse and Williams, Does Index Speculation Impact Commodity Prices?, Financial Review, Vol. 48, Issue 3 (2013); Tse, The Relationship Among Agricultural Futures, ETFs, and the US Stock Market, Review of Futures Markets (2012); Varadi, An Evidence of Speculation in Indian Commodity Markets (working paper 2012); Williams, Dodging Dodd-Frank: Excessive Speculation, Commodities Markets, and the Burden of Proof, Law & Policy Journal of the University of Denver (2015).

[241] Studies that employ the comovement or cointegration methods include: Adämmer, Bohl and Stephan, Speculative Bubbles in Agricultural Prices (working paper 2011); Algieri, A Roller Coaster Ride: an Empirical Investigation of the Main Drivers of Wheat Price (working paper 2013); Babula and Rothenberg, A Dynamic Monthly Model of U.S. Pork Product Markets: Testing for and Discerning the Role of Hedging on Pork-Related Food Costs, Journal of Int'l Agricultural Trade and Development (2013); Baffes and Haniotos, Placing the 2006/08 Commodity Boom into Perspective, World Bank Policy Research Working Paper 5371 (2010); Basu and Miffre, Capturing the Risk Premium of Commodity Futures: The Role of Hedging Pressure, Journal of Banking and Risk (2013); Belke, Bordon, and Volz, Effects of Global Liquidity on Commodity and Food Prices, German Institute for Economic Research (2013); Bicchetti and Maystre, The Synchronized and Long-lasting Structural Change on Commodity Markets: Evidence from High Frequency Data (working paper 2012); Boyd, Büyükşahin, and Haigh, The Prevalence, Sources, and Effects of Herding (working paper 2013); Bunn, Chevalier, and Le Pen, Fundamental and Financial Influences on the Co-movement of Oil and Gas Prices (working paper 2012); Büyükşahin, Harris, and Haigh, Fundamentals, Trader Activity, and Derivatives Pricing (working paper 2008); Büyükşahin and Robe, Does it Matter Who Trades Energy Derivatives?, Review of Env't, Energy, and Economics (2013); Büyükşahin and Robe, Does ''Paper Oil'' Matter? (working paper 2011); Büyükşahin and Robe, Speculators, Commodities, and Cross-Market Linkages (working paper 2012); Cheng, Kirilenko, and Xiong, Convective Risk Flows in Commodity Futures Markets (working paper 2012); Coleman and Dark, Economic Significance of Non-Hedger Investment in Commodity Markets (working paper 2012); Creti, Joets, and Mignon, On the Links Between Stock and Commodity Markets' Volatility, Energy Economics (2010); Dorfman and Karali, Have Commodity Index Funds Increased Price Linkages between Commodities? (working paper 2012); Filimonov, Bicchetti, Maystre, and Sornette, Quantification of the High Level of Endogeneity and of Structural Regime Shifts in Commodity Markets, (working paper 2013); Haigh, Harris, and Overdahl, Market Growth, Trader Participation and Pricing in Energy Futures Markets (working paper 2007); Hoff, Herding Behavior in Asset Markets, Journal of Financial Stability (2009); Kawamoto, Kimura, *et al.,* What Has Caused the Surge in Global Commodity Prices and Strengthened Cross-market Linkage?, Bank of Japan Working Papers Series No.11–E–3 (May 2011); Korniotis, Does Speculation Affect Spot Price Levels? The Case of Metals With and Without Futures Markets (working paper, FRB Finance and Economic Discussion Series 2009); Le Pen and Sévi, Futures Trading and the Excess Comovement of Commodity Prices (working paper 2012); Pollin and Heintz, How Wall Street Speculation is Driving Up Gasoline Prices Today (AFR working paper 2011); Tang and Xiong, Index Investment and Financialization of Commodities, Financial Analysts Journal (2012); and Windawi, Speculation, Embedding, and Food Prices: A Cointegration Analysis (working paper 2012).

[242] Studies that employ models of fundamental supply and demand include: Acharya, Ramadorai, and Lochstoer, Limits to Arbitrage and Hedging: Evidence from Commodity Markets, Journal of Financial Economics (2013); Allen, Litov, and Mei, Large Investors, Price Manipulation, and Limits to Arbitrage: An Anatomy of Market Corners, Review of Finance (2006); Bos and van der Molen, A Bitter Brew? How Index Fund Speculation Can Drive Up Commodity Prices, Journal of Agricultural and Applied Economics (2010); Breitenfellner, Crespo, and Keppel, Determinants of Crude Oil Prices: Supply, Demand, Cartel, or Speculation?, Monetary Policy and the Economy (2009); Brennan and Schwartz, Arbitrage in Stock Index Futures, Journal of Business (1990); Byun and Sungje, Speculation in Commodity Futures Market, Inventories and the Price of Crude Oil (working paper 2013); Chan, Trade Size, Order Imbalance, and Volatility-Volume Relation, Journal of Financial Economics (2000); Chordia, Subrahmanyam and Roll, Order imbalance, Liquidity, and Market Returns, Journal of Financial Economics (2002); Cifarelli and Paladino, Oil Price Dynamics and Speculation: a Multivariate Financial Approach, Energy Economics (2010); Doroudian and Vercammen, First and Second Order Impacts of Speculation and Commodity Price Volatility (working paper 2012); Ederington, Dewally, and Fernando, Determinants of Trader Profits in Futures Markets (working paper 2013); Einloth, Speculation and Recent Volatility in the Price of Oil (working paper 2009); Frankel and Rose, Determinants of Agricultural and Mineral Commodity Prices (working paper 2010); Girardi, Do Financial Investors Affect Commodity Prices? (working paper 2011); Gorton, Hayashi, Rouwenhorst, The Fundamentals of Commodity Futures Returns, Review of Finance (2013); Guilleminot and Ohana, The Interaction of Hedge Funds and Index Investors in Agricultural Derivatives Markets (working paper 2013); Gupta and Kamzemi, Factor Exposures and Hedge Fund Operational Risk: The Case of Amaranth (working

Some economists have developed economic models for the supply and demand of a commodity. These models often include theories of how storage capacity and use affect supply and demand, which may influence the price of a physical commodity over time. An economist looks at where the model is in equilibrium with respect to quantities of a commodity supplied and demanded to arrive at a ''fundamental'' price or price return. The economist then looks for deviations between the fundamental price (based on the model) and the actual price of a commodity. When there is a statistically significant deviation between the fundamental price and the actual price, the economist generally infers that the price is not driven by market fundamentals of supply and demand.

Switching Regressions or Similar Analyses [243]

In the context of studies relating to position limits, economists employing switching regression analysis generally posit a model with two states: A normal state, where prices reflect market fundamentals, and a second state, often interpreted as a ''bubble.'' [244] Using price data, authors of these studies calculate the probability of a transition between the two states. The point of transition is called a structural ''breakpoint.'' Examination of these breakpoints permits the researcher to identify the duration of a particular ''bubble.''

Eigenvalue Stability Analysis [245]

Some economists have run regression analyses [246] on price and time-lagged values of price. They estimate an equation that relates current to past time values over short time intervals and solve for the roots of that equation, called the eigenvalues (latent values), in order to detect unusual price changes. If they find an eigenvalue [247] with an absolute value of greater than one, they infer that the price of the commodity is in a ''bubble.''

Theoretical Models [248]

paper 2009); Haigh, Hranaiova, and Overdahl, Hedge Funds, Volatility, and Liquidity Provisions in the Energy Futures Markets, Journal of Alternative Investments (2007); Haigh, Hranaiova, and Overdahl, Price Dynamics, Price Discovery, and Large Futures Trader Interactions in the Energy Complex, (working paper 2005); Hamilton, Causes and Consequences of the Oil Shock of 2007–2008, Brookings Paper on Economic Activity (2009); Hamilton and Wu, Effects of Index-Fund Investing on Commodity Futures Prices, International Economic Review, Vol. 56, No. 1 (2015); Hamilton and Wu, Risk Premia in Crude Oil Futures Prices, Journal of International Money and Finance (2013); Harrison and Kreps, *Speculative Investor Behavior in a Stock Market with Heterogeneous Expectations,* Quarterly Journal of Economics (1978); Henderson, Pearson and Wang, New Evidence on the Financialization of Commodity Markets (working paper 2012); Hirshleifer, Residual Risk, Trading Costs, and Commodity Futures Risk Premia, Review of Financial Studies, Vol. 1, No. 2, Oxford University Press (1988); Hong and Yogo, Digging into Commodities (working paper 2009); Interagency Task Force on Commodity Markets, Interim Report on Crude Oil, multiple federal agencies including the CFTC (2008); Juvenal and Petrella, Speculation in the Oil Market (working paper 2012); Juvenal and Petrella, Speculation in Commodities, and Cross-Market Linkages (working paper 2011); Kilian, Not All Oil Price Shocks Are Alike: Disentangling Demand and Supply Shocks in the Crude Oil Market, American Economic Review (2007); Kilian and Lee, Quantifying the Speculative Component in the Real Price of Oil: The Role of Global Oil Inventories (working paper 2013); Kilian and Murphy, The Role of Inventories and Speculative Trading in the Global Market for Crude Oil, Journal of Applied Econometrics (2010); Knittel and Pindyck, The Simple Economics of Commodity Price Speculation, (working paper 2013); Kyle and Wang, Speculation Duopoly with Agreement to Disagree: Can Overconfidence Survive the Market Test?, Journal of Finance (1997); Manera, Nicolini and Vignati, Futures Price Volatility in Commodities Markets: The Role of Short-Term vs Long-Term Speculation (working paper 2013); Mei, Acheinkman, and Xiong, Speculative Trading and Stock Prices: An Analysis of Chinese A–B Share Premia, Annals of Economics and Finance (2009); Morana, Oil Price Dynamics, Macro-finance Interactions and the Role of Financial Speculation, Journal of Banking & Finance, Vol. 37, Issue 1 (Jan. 2012); Mou, Limits to Arbitrage and Commodity Index Investment: Front-Running the Goldman roll (working paper 2011); Plato and Hoffman, Measuring the Influence of Commodity Fund Trading on Soybean Price Discovery (working paper 2007); Sornette, Woodard and Zhou, The 2006–2008 Oil Bubble and Beyond: Evidence of Speculation, and Prediction, Physica A. (2009); Stevans and Sessions, Speculation, Futures Prices, and the U.S. Real Price of Crude Oil, American Journal of Social and Management Science (2010); Trostle, Global Agricultural Supply and Demand: Factors Contributing to the Recent Increase in Food Commodity Prices, USDA Economic Research Service (2008);Van der Molen, Speculators Invading the Commodity Markets (working paper 2009); Weiner, Do Birds of A Feather Flock Together? Speculation in the Oil Markets, (Working Paper 2006); Weiner, Speculation in International Crises: Report from the Gulf, Journal of Int'l Business Studies (2005); Westcott and Hoffman, Price Determination for Corn and Wheat: The Role of Market Factors and Government Programs (working paper 1999); Wright, International Grain Reserves and Other Instruments to Address Volatility in Grain Markets, World Bank Research Observer (2012).

[243] Studies that include switching regressions or similar analyses include: Brooks, Prokopczuk, and Wu, *Boom and Bust in Commodity Markets: Bubbles or Fundamentals?* (working paper 2014); Baldi and Peri, Price Discovery in Agricultural Commodities: the Shifting Relationship Between Spot and Futures Prices (working paper 2011); Chevallier, Price Relationships in Crude oil Futures: New Evidence from CFTC Disaggregated Data, Environmental Economics and Policy Studies (2012); Cifarelli and Paladino, Commodity Futures Returns: A non-linear Markov Regime Switching Model of Hedging and Speculative Pressures (working paper 2010); Fan and Xu, What Has Driven Oil Prices Since 2000? A Structural Change Perspective, Energy Economics (2011); Hache and Lantz, Speculative Trading & Oil Price Dynamic: A Study of the WTI Market, Energy Economics, Vol. 36, p.340 (March 2013); Lammerding, Stephan, Trede, and Wifling, Speculative Bubbles in Recent Oil Price Dynamics: Evidence from a Bayesian Markov Switching State-Space Approach, Energy Economics Vol. 36 (2013); Sigl-Grüb and Schiereck, Speculation and Nonlinear Price Dynamics in Commodity Futures Markets, Investment Management and Financial Innovations, Vol. 77 (2010); Silvernnoinen and Thorp, Financialization, Crisis and Commodity Correlation Dynamics, Journal of Int'l Financial Markets, Institutions, and Money (2013).

[244] While there is no broad academic consensus on the formal, testable economic definition of the term ''price bubble,'' price bubbles are colloquially thought to be unsustainable surges in asset prices fueled by speculation and followed by ''crashes'' or precipitous price drops.

[245] Studies that employ eigenvalue stability analysis include: Czudaj and Beckman, Spot and Futures Commodity Markets and the Unbiasedness Hypothesis—Evidence from a Novel Panel Unit Root Test, Economic Bulletin (2013); Du, Yu, and Hayes, Speculation and Volatility Spillover in the Crude Oil and Agricultural Commodity Markets: A Bayesian Analysis, (working paper 2012); Gilbert, *Speculative Influences on Commodity Futures Prices, 2006–2008,* UN Conference on Trade and Development (working paper 2010); Gutierrez, Speculative Bubbles in Agricultural Commodity Markets, European Review of Agricultural Economics (2012); Phillips and Yu, Dating the Timeline of Financial Bubbles During the Subprime Crisis, Quantitative Economics (2011).

[246] In statistical modeling, regression analysis is a process for estimating the relationships among certain types of variables (values that change over time or in different circumstances).

[247] In this context, an eigenvalue is a mathematical calculation that summarizes the dynamic properties of the data generated by the model. Generally, an eigenvalue is a concept from linear algebra.

[248] Studies that present theoretical models include: Avriel and Reisman, Optimal Option Portfolios in Markets with Position Limits and Margin Requirements, Journal of Risk (2000); Dai, Jin and Liu, Illiquidity, Position Limits, and Optimal Investment (working paper 2009); Dicembrino and Scandizzo, The Fundamental and Speculative Components of the Oil Spot Price: A Real Options Value Approach (working paper 2012); Dutt and Harris, Position Limits for Cash-Settled Derivative Contracts, Journal of Futures Markets (2005); Ebrahim and ap Gwilym, Can Position Limits Restrain Rogue Traders?, at p.832 Journal of Banking & Finance (2013); Edirsinghe, Naik, and Uppal, Optimal Replication of Options with Transaction Costs and Trading Restrictions, Journal of Financial and Quantitative Analysis (1993); Froot, Scharfstein, and Stein, Herd on the Street: Informational Inefficiencies in a Market with Short Term Speculation, (Working Paper 1990); Kumar and Seppi, Futures Manipulation with ''Cash Settlement'', Journal of Finance (1992); Kyle and Viswanathan, How to Define Illegal Price Manipulation, American Economic Review (2008); Kyle and Wang, Speculation Duopoly with Agreement to Disagree: Can Overconfidence Survive the Market Test?, Journal of Finance (1997); Lee, Cheng and Koh, An Analysis of Extreme Price Shocks and Illiquidity Among Systematic Trend Followers (working paper 2010); Leitner, Inducing Agents to Report Hidden Trades: A Theory of an Intermediary, Review of Finance (2012); Liu, Financial-Demand Based Commodity Pricing: A Theoretical Model for Financialization of Commodities (working paper 2011); Lombardi and van Robays, Do Financial Investors Destabilize the

Continued

Some studies perform little or no empirical analysis and instead present a general theoretical model that may bear, directly or indirectly, on the effect of excessive speculation in the commodities markets. Because these papers do not include empirical analysis, they contain many untested assumptions and conclusory statements, limiting their usefulness to the Commission.

Surveys of Economic Literature and Opinion Pieces [249]

The Commission considered more than seventy studies that are survey or opinion pieces. Some of these studies provide useful background material but, on the whole, they offer mere opinion unsupported by rigorous empirical analysis. While they may be useful for developing hypotheses or informing policymakers, these secondary sources often exhibit policy bias and are not neutral, reliable bases for scientific inquiry the way that primary economic studies are.[250]

More Persuasive Academic Studies

While the economic literature is inconclusive, the Commission can

Oil Price? (working paper, European Central Bank, 2011); Morris, Speculative Investor Behavior and Learning, Quarterly Journal of Economics (1996); Parsons, Black Gold & Fool's Gold: Speculation in the Oil Futures Market, Economia (2009); Pierru and Babusiaux, Speculation without Oil Stockpiling as a Signature: A Dynamic Perspective (working paper 2010); Pirrong, Manipulation of the Commodity Futures Market Delivery Process, Journal of Business (1993); Pirrong, The Self-Regulation of Commodity Exchanges: The Case of Market Manipulation, Journal of Law and Economics (1995); Pliska and Shalen, The Effects of Regulation on Trading Activity and Return Volatility in Futures Markets, Journal of Futures Markets (2006); Routledge, Seppi, and Spatt, Equilibrium Forward Curves for Commodities, Journal of Finance (2000); Schulmeister, Technical Trading and Commodity Price Fluctuations (working paper 2012); Schulmeister, Torero, and von Braun, Trading Practices and Price Dynamics in Commodity Markets (working paper 2009); Shleifer and Vishney, The Limits of Arbitrage, Journal of Finance (1997); Sockin and Xiong, Feedback Effects of Commodity Futures Prices (working paper 2012); Vansteenkiste, What is Driving Oil Price Futures? Fundamentals Versus Speculation (working paper, European Central Bank, 2011); Westerhoff, Speculative Markets and the Effectiveness of Price Limits, Journal of Economic Dynamics and Control (2003).

[249] Studies that are survey or opinion pieces include: Anderson, Outlaw, and Bryant, The Effects of Ethanol on Texas Food and Feed, Agricultural and Food Policy Center Research Report (2008); Baffes, The Long-term Implications of the 2007–2008 *Commodity-Price Boom,* Development in Practice (2011); Basu and Gavin, What Explains the Growth in Commodity Derivatives? (working paper 2011); Berg, The Rise of Commodity Speculation: from Villainous to Venerable, (2011); Bessenbinder, Lilan, and Mahadeva, The Role of Speculation in Oil Markets: What Have We Learned So Far? (working paper 2012); Cagan, Financial Futures Markets: Is More Regulation Needed?, Journal of Futures Markets (1981); Chincarini, The Amaranth Debacle: Failure of Risk Measures or Failure of Risk Management (working paper 2007); Chincarini, Natural Gas Futures and Spread Position Risk: Lessons from the Collapse of Amaranth Advisors L.L.C., Journal of Applied Finance (2008); CME Group, Inc., Excessive Speculation and Position Limits in Energy Derivatives Markets (working paper); Cooper, Excessive Speculation and Oil Price Shock Recessions: A Case of Wall Street ''Déjà vu All Over Again,'' Consumer Federation of America (2011); Dahl, Future Markets: The Interaction of Economic Analyses and Regulation: Discussion, American Journal of Agricultural Economics (1980); De Schutter, Food Commodities Speculation and Food Price Crises, United Nations Special Report on the Right to Food (2010); Easterbrook, Monopoly, Manipulation, and the Regulation of Futures Markets, Journal of Business (1986); Eckaus, The Oil Price Really is a Speculative Bubble (working paper 2008); Ellis, Michaely, and O'Hara, The Making of a Dealer Market: From Entry to Equilibrium in the Trading of Nasdaq Stocks, Journal of Finance (2002); European Commission, Review of the Markets in Financial Instruments Directive (working paper 2010); European Commission, Tackling the Challenges in Commodity Markets, Communication from the European Commission to the European Parliament (2011); Frenk and Turbeville, Commodity Index Traders and the Boom/Bust Cycle in Commodities Prices, Better Markets Copyright (2011); Goldman Sachs, Global Energy Weekly March 2011 (2011); Government Accountability Office, Issues Involving the Use of the Futures Markets to Invest in Commodity Indexes, (Report 2009); Greenberger, The Relationship of Unregulated Excessive Speculation to Oil Market Price Volatility (working paper 2010); Harris, Circuit Breaker and Program Trading Limits: What Have We Learned, Brooking Institutions Press (1997); Henn, CL–WEED–59628; Her Majesty's Treasury, Global Commodities: A Long Term Vision for Stable, Secure, and Sustainable Global Markets, (2008); House of Commons Select Committee on Science & Technology of the United Kingdom, Strategically Important Metals, (2011); Hunt, Thought for the Day: Unreported Copper Stocks, Simon Hunt Strategic Services (2011); Inamura Kimata, and Takeshi, Recent Surge in Global commodity Prices—Impact of Financialization of Commodities and Globally Accommodative Monetary Conditions, Bank of Japan Review March 2011; International Monetary Fund, Is Inflation Back? Commodity Prices and Inflation, Chapter 3 of IMF's World Economic Outlook ''Financial Stress, Downturns, and Recoveries'' (2008); Irwin and Sanders, Index Funds, Financialization, and Commodity Futures Markets, Applied Economic Perspective and Policy (2010); Jack, Populists vs Theorists: Futures Markets and the Volatility of Prices, Exploration in Economic History (2006); Jickling and Austin, Hedge Fund Speculation and Oil Prices (working paper 2011); Kemp, Crisis Remarks the Commodity Business, Reuters Columnist (2008); Khan, The 2008 Oil Price ''Bubble (working paper 2009); Koski and Pontiff, How Are Derivatives Used? 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(working paper 2012); Pirrong, Squeezes, Corners, and the Anti-Manipulation Provisions of the Commodity Exchange Act, Regulation (1994); Pirrong, Annex B to CL–ISDA/SIFMA–59611; Plante and Yucel, Did Speculation Drive Oil Prices? Market Fundamentals Suggest Otherwise, Federal Reserve Bank of Dallas (2011); Plante and Yucel, Did Speculation Drive Oil Prices? 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[250] For example, these surveys may posit ''facts'' that are unsupported by testing, may not test their hypotheses, or may claim results that are subject to multiple interpretations.

identify a few of the well-executed studies that do not militate against and, to some degree, support the Commission's reproposal to follow, out of due caution, a prophylactic approach.[251] Hamilton and Wu, in *Risk Premia in Crude Oil Futures Prices,* Journal of International Money and Finance (2013), using models of fundamental supply and demand, find evidence that changes in non-commercial positions can affect the risk premium in crude oil futures prices; that is, Hamilton and Wu found that, for a limited period around the time of the 2008 financial crisis that gave rise to the Dodd-Frank Act, increases in speculative positions reduced the risk premiums[252] in crude oil futures prices.[253] This is important because, all else being equal, one would expect the risk premium to be the component of price that would be affected by traders accumulating large positions.[254] Hamilton, in *Causes of the Oil Shock of 2007–2008,* Brookings Paper on Economic Activity (2009), also concludes that the oil price run-up was caused by strong demand confronting stagnating world production, but that something other than fundamental factors of supply and demand (as modeled) may have aggravated the speed and magnitude of the ensuing oil price collapse. Singleton, in *Investor Flows and the 2008 Boom/Bust in Oil Prices* (working paper 2011), employs a technique that is similar to Granger causality and finds a negative correlation between speculative positions and risk premiums.[255] Chevallier, in *Price Relationships in Crude Oil Futures: New Evidence from CFTC Disaggregated Data,* Environmental Economics and Policy Studies (2012), applies switching regression analysis to position data and concludes that one cannot eliminate the possibility of speculation as one of the main factors contributing to oil price volatility in 2008. This study also suggests that when supply and demand are highly inelastic, *i.e.,* relatively unresponsive to price changes, financial investors may have contributed to oil price volatility by taking large positions in energy sector commodity index funds.[256] As one may infer from this small sample, some of the more compelling studies that support the proposition that large positions may move prices involve empirical studies of the oil market. The Commission acknowledges that not all commodity markets exhibit the same price behavior at the same times. Even so, that the findings of a particular study of the market experience of a particular commodity over a particular time period may not be extensible to other commodity markets or over other time periods does not mean that the Commission should disregard that study. This is because, as explained elsewhere, these markets are over time all susceptible to similar risks from excessive speculation. Again, this supports a prophylactic approach to limits and a determination that limits are necessary to effectuate their statutory purposes.

The Commission in the December 2013 Position Limits Proposal identified two studies of actual market events to be helpful and persuasive in making its alternative necessity finding:[257] The inter-agency report on the silver crisis[258] and the PSI Report on Excessive Speculation in the Natural Gas Market.[259] These two studies and some of the other reports included in the survey category[260] do not use statistical or theoretical models to reach economically rigorous conclusions. Some of the evidence cited in these studies is anecdotal. Still, these two studies are in-depth examinations of actual market events and the Commission continues to find them to be helpful and persuasive in making its preliminary alternative necessity finding. The Commission reiterates that the PSI Report (because it closely preceded Congress' amendments to CEA section 4a(a) in the Dodd-Frank Act) indicates how Congress views limits as necessary as a prophylactic measure to prevent the adverse effects of excessively large speculative positions. The studies, individually or taken as a whole, do not dissuade the Commission from its consistent view that large speculative positions and outsized market power pose risks to well-functioning commodities markets, nor from its preliminary finding that speculative position limits are necessary to achieve their statutory purposes.

The Commission requests comment on its discussion of studies and reports. It also invites commenters to advise the Commission of any additional studies that the Commission should consider, and why.

## II. Compliance Date for the Reproposed Rules

Commenters requested that the Commission delay the compliance date, generally for at least nine months, to provide adequate time for market participants to come into compliance with a final rule.[261] In addition, a commenter requested the Commission delay the compliance date until no earlier than January 3, 2018, to coordinate with the expected implementation date for position limits in Europe.[262]

In response to commenters, in this reproposal, the Commission proposes to delay the compliance date of any final rule until, at earliest, January 3, 2018, as provided under reproposed § 150.2(e). The Commission is of the opinion that a delay would provide market participants with sufficient time to come into compliance with a final rule, particularly in light of grandfathering provisions, discussed below.

The Commission believes that a delay until January 3, 2018, would provide time for market participants to gain

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[251] Generally, studies that the Commission considers to be well-executed, for example, employ well-accepted, defensible, scientific methodology, document and present facts and results that can be replicated, are on point regarding issues relevant to position limits, and may eventually appear in respected, peer-reviewed academic journals.

[252] A risk premium is the amount of return on a particular asset or investment that is in excess of the expected rate of return on a theoretically risk free asset or investment, *i.e.,* one with a virtually certain or guaranteed return.

[253] The economic rationale behind this is that speculative traders would be taking long positions to earn the risk premium, among other things. If more speculative traders are going long, *i.e.,* bidding to earn the risk premium, the risk premium would be reduced. In this way, speculators make it cheaper for short hedgers to lock in their price risk. *Contra* Harris and Büyükşahin, The Role of Speculators in the Crude Oil Futures Market (working paper 2009) (concluding that price changes precede the position change). In this way, speculators make it cheaper for short hedgers to lock in their price risk.

[254] Long speculators would tend to be compensated for assuming the price risk that is inherent with going long in the crude oil futures contract. If more speculators are bidding to earn the risk premium by taking long position in crude oil futures contracts, it should lower the risk premium, all else being equal.

[255] That is, when long speculative positions are larger, the risk premiums are smaller.

[256] *See also* Hamilton and Wu, *Risk Premia in Crude Oil Futures Prices,* Journal of International Money and Finance (2013); Hamilton, *Causes of the Oil Shock of 2007–2008,* Brookings Paper on Economic Activity (2009).

[257] December 2013 Position Limits Proposal, 78 FR at 75695–6.

[258] U.S. Commodity Futures Trading Commission, ''Part Two, A Study of the Silver Market,'' May 29, 1981, Report to Congress in Response to Section 21 of The Commodity Exchange Act.

[259] U.S. Senate Permanent Subcommittee on Investigations, ''Excessive Speculation in the Natural Gas Market,'' June 25, 2007.

[260] *E.g.,* U.S. Commodity Futures Trading Commission, Staff Report on Commodity Swap Dealers and Index Traders with Commission Recommendations (2008); U.S. Senate Permanent Subcommittee, Excessive Speculation in the Wheat Market (2009); U.S. Senate Permanent Subcommittee, The Role of Market Speculation in Rising Oil and Gas Prices: A Need to Put the Cop Back on the Beat (2006).

[261] *See, e.g.,* CL–FIA–60937 at 5.

[262] CL–FIA–61036 at 2.

access to adequate systems to compute futures-equivalent positions. The Commission bases this opinion on its experience, including with swap dealers and clearing members of derivative clearing organizations, who, as reporting entities under part 20 (swaps large trader reporting), have been required to prepare reports of swaps on a futures-equivalent basis for years. As discussed above, futures-equivalent reporting of swaps under part 20 generally has improved. This means many reporting entities already have implemented acceptable systems to compute futures-equivalent positions. The systems developed for that purpose also should be acceptable for monitoring compliance with position limits. The Commission believes it is reasonable to expect some reporting entities to offer futures-equivalent computation services to market participants. In this regard, such reporting entities already compute and report, under part 20, futures-equivalent positions for swap counterparties with reportable positions, including spot-month positions and non-spot-month positions.

The Commission notes that market participants who expect to be over the limits would need to assess whether exemptions are available (including requesting non-enumerated bona fide hedging positon exemptions or spread exemptions from exchanges, as discussed below under reproposed §§ 150.9 and 150.10). In the absence of exemptions, such market participants would need to develop plans for coming into compliance.

The Commission notes the request for a further delay in a compliance date may be mitigated by the grandfathering provisions in the Reproposal. First, the reproposed rules would exclude from position limits ''pre-enactment swaps'' and ''transition period swaps,'' as discussed below. Second, the rules would exempt certain pre-existing positions from position limits under reproposed § 150.2(f). Essentially, this means only futures contracts initially would be subject to non-spot-month position limits, as well as swaps entered after the compliance date. The Commission notes that a pre-existing position in a futures contract also would not be a violation of a non-spot-month limit, but, rather, would be grandfathered, as discussed under reproposed § 150.2(f)(2), below. Nevertheless, the Commission intends to provide a substantial implementation period to ease the compliance burden.

The Commission requests comment on its discussion of the proposed compliance date.

## III. Reproposed Rules

The Commission is not addressing comments that are beyond the scope of this reproposed rulemaking.

### *A. § 150.1—Definitions*

1. Various Definitions Found in § 150.1

Among other elements, the December 2013 Position Limits Proposal included amendments to the definitions of ''futures-equivalent,'' ''long position,'' ''short position,'' and ''spot-month'' found in § 150.1 of the Commission's regulations, to conform them to the concepts and terminology of the CEA, as amended by the Dodd-Frank Act. The Commission also proposed to add to § 150.1, definitions for ''basis contract,'' ''calendar spread contract,'' ''commodity derivative contract,'' ''commodity index contract,'' ''core referenced futures contract,'' ''eligible affiliate,'' ''entity,'' ''excluded commodity,'' ''intercommodity spread contract,'' ''intermarket spread positions,'' ''intramarket spread positions,'' ''physical commodity,'' ''pre-enactment swap,'' ''pre-existing position,'' ''referenced contract,'' ''spread contract,'' ''speculative position limit,'' ''swap,'' ''swap dealer'' and ''transition period swap.'' In addition, the Commission proposed to move the definition of bona fide hedging from § 1.3(z) into part 150, and to amend and update it. Moreover, the Commission proposed to delete the definition for ''the first delivery month of the 'crop year.' '' [263] Separately, the Commission proposed making a non-substantive change to list the definitions in alphabetical order rather than by use of assigned letters.[264] According to the December 2013 Position Limits Proposal, this last change would be helpful when looking for a particular definition, both in the near future, in light of the additional definitions proposed to be adopted, and in the expectation that future rulemakings may adopt additional definitions.

Finally, in connection with the 2016 Supplemental Position Limits Proposal, which provided new alternative processes for DCMs and SEFs to recognize certain positions in commodity derivative contracts as non-enumerated bona fide hedges or enumerated anticipatory bona fide hedges, and to exempt from federal position limits certain spread positions, the Commission proposed to further amend certain relevant definitions, including changes to the definitions of ''futures-equivalent,'' ''intermarket spread position,'' and ''intramarket spread position.''

Separately, as noted in the December 2013 Position Limits Proposal, amendments to two definitions were proposed in the November 2013 Aggregation Proposal,[265] which was approved by the Commission on the same date as the December 2013 Position Limits Proposal. The November 2013 Aggregation Proposal, a companion to the December 2013 Position Limits Proposal, included amendments to the definitions of ''eligible entity'' and ''independent account controller.'' [266] The Commission notes that since the amendments were part of the separate Aggregation proposal, the proposed amendments to those definitions, and comments thereon, are addressed in the final Aggregation rulemaking (the ''2016 Final Aggregation Rule''); [267] therefore, the Commission is not addressing the definitions of ''eligible entity'' and ''independent account controller'' herein.

The Commission is reproposing the amendments to the definitions in § 150.1, as set forth in the December 2013 Position Limits Proposal and as amended in the 2016 Supplemental Position Limits Proposal, with modifications made in response to public comments. The Reproposal also includes non-substantive changes to certain definitions to enhance readability and clarity for market participants and the public, including the extraction of definitions that were contained in the definition of ''referenced contract'' to stand on their own. The amendments and the public

[263] At that time, the Commission noted that several terms that are not currently in part 150 were not included in the December 2013 Position Limits Proposal even though definitions for those terms were adopted in vacated part 151. The Commission stated its view that the definition of those terms was not necessary for clarity in light of other revisions proposed in that rulemaking. The terms not proposed at that time include ''swaption'' and ''trader.''

[264] The December 2013 Position Limits Proposal also made several non-substantive edits to the definitions to make them easier to read.

[265] *See* Aggregation of Positions, 78 FR 68946 (Nov. 15, 2013) at 68965, 68974 (proposing changes to the definitions of ''eligible entity'' and ''independent account controller'') (''November 2013 Aggregation Proposal''). The Commission issued a supplement to this proposal in September 2015, but the supplement did not propose any changes to the definitions. *See* 80 FR 58365 (Sept. 29, 2015).

[266] The December 2013 Position Limits Proposal mirrored the amendments to the definitions of ''eligible entity'' and ''independent account controller,'' proposed in the November 2013 Aggregation Proposal, and also included some non-substantive change to the definition of ''independent account controller.''

[267] *See* 2016 Final Aggregation Rule, adopted by the Commission separately from this Reproposal.

comments relevant to each amendment are discussed below.

a. Basis Contract

*Proposed Rule:* In the December 2013 Position Limits Proposal, the Commission proposed to exclude ''basis contracts'' from the definition of ''referenced contracts.'' [268] While the term ''basis contract'' is not defined in current § 150.1, the Commission proposed a definition for basis contract in the December 2013 Position Limits Proposal. Proposed § 150.1 defined basis contract to mean ''a commodity derivative contract that is cash-settled based on the difference in: (1) The price, directly or indirectly, of: (a) A particular core referenced futures contract; or (b) a commodity deliverable on a particular core referenced futures contract, whether at par, a fixed discount to par, or a premium to par; and (2) the price, at a different delivery location or pricing point than that of the same particular core referenced futures contract, directly or indirectly, of: (a) A commodity deliverable on the same particular core referenced futures contract, whether at par, a fixed discount to par, or a premium to par; or (b) a commodity that is listed in appendix B to this part as substantially the same as a commodity underlying the same core referenced futures contract.''

The Commission also proposed Appendix B to part 150, Commodities Listed as Substantially the Same for Purposes of the Definition of Basis Contract. As proposed, the definition of basis contract would include contracts cash-settled on the difference in prices of two different, but economically closely related commodities, for example, certain quality differentials (*e.g.,* RBOB gasoline vs. 87 unleaded).[269] As explained when it was proposed, the intent of the proposed definition was to reduce the potential for excessive speculation in referenced contracts where, for example, a speculator establishes a large outright directional position in referenced contracts and nets down that directional position with a contract based on the difference in price of the commodity underlying the referenced contracts and a close economic substitute that was not deliverable on the core referenced futures contract.[270] In the absence of this provision, the speculator could then increase further the large position in the referenced contracts. By way of comparison, the Commission noted in the December 2013 Position Limits Proposal that there is greater concern (i) that someone may manipulate the markets by disguise of a directional exposure through netting down the directional exposure using one of the legs of a quality differential (if that quality differential contract were not exempted), than (ii) that someone may use certain quality differential contracts that were exempted from position limits to manipulate the outright price of a referenced contract.[271]

*Comments Received:* The Commission received a number of comment letters regarding the proposed definition of basis contract. One commenter supported the proposed definition of basis contract and stated that it appreciates the Commission's inclusion of Appendix B listing the commodities it believes are substantially the same as a core referenced futures contract for purposes of identifying contracts that meet the basis contract definition.[272] Other comment letters requested that the Commission broaden the definition to include contracts that settle to other types of differentials, such as processing differentials (*e.g.,* crack or crush spreads) or quality differentials (*e.g.,* sweet vs. sour crude oil). One commenter recommended a definition of basis contract that includes crack spreads, by-products priced at a differential to other by-products (*e.g.,* jet fuel vs. heating oil, both of which are crude oil by-products), and a commodity that includes similar commodities such as a contract based on the difference in prices between light sweet crude and a sour crude that is not deliverable against the NYMEX Light Sweet Crude Oil core referenced futures contract. This commenter suggested that if these types of contracts are included as basis contracts, market participants should be able to net certain contracts where a commodity is priced at a differential to a product or by-product, subject to prior approval according to a process created by the Commission.[273]

Two commenters specifically requested that the list in Appendix B include Jet fuel (54 grade) as substantially the same as heating oil (67 grade). They also requested that WTI Midland (Argus) vs. WTI Financial Futures should be listed as basis contracts for Light Louisiana Sweet (LLS) Crude Oil.[274]

Noting that basis contracts are excluded from the definition of referenced contract and thus not subject to speculative position limits, two commenters requested CFTC expand the list in Appendix B to part 150 of commodities considered substantially the same as a core referenced futures contract, and the corresponding list of basis contracts, to reflect the commercial practices of market participants.[275] One of these commenters recommended that the Commission adopt a flexible process for identifying any additional commodities that are substantially the same as a commodity underlying a core referenced futures contract for inclusion in Appendix B, and allow market participants to request a timely interpretation regarding whether a particular commodity is substantially the same as a core referenced futures contract or that a particular contract qualifies as a basis contract.[276]

*Commission Repropsal:* The Commission has determined to repropose the definition of basis contract as originally proposed, but to change the defined term from ''basis contract'' to ''location basis contract.'' The Commission intended the ''basis contract'' definition to encompass contracts that settle to the difference between prices in separate delivery locations of the same (or substantially the same) commodity, while the industry seems to use the term ''basis'' more broadly to include other price differentials, including, among other things, processing differentials and quality differentials. Thus, under the Reproposal, the term is changing from ''basis contract'' to ''location basis contract'' in order to reduce any confusion stemming from the more encompassing use of the word ''basis'' in industry parlance.[277]

[268] The Commission also notes that the proposed definition of ''commodity index contract'' excluded intercommodity spread contracts, calendar spread contracts, and basis contracts.

[269] The proposed basis contract definition was not intended to include significant time differentials in prices of the two commodities (*e.g.,* the proposed basis contract definition did not include calendar spreads for nearby vs. deferred contracts).

[270] December 2013 Position Limits Proposal at 75696.

[271] *Id.*

[272] CL–Working Group–59693 at 68.

[273] CLWorking Group–59959 at 16.

[274] CL–FIA–59595 at 19; CL–ISDA/SIFMA–59611 at 35.

[275] CL–FIA–59595 at 4 and 18–19; CL–ISDA/SIFMA–59611 at 34–35.

[276] CL–FIA–59595 at 19.

[277] Consequently, the Commission realizes that its determination to retain its traditional definition while clarifying its meaning by adopting the amended term of ''locational basis contract'' does not provide for the expanded definition of basis contract requested by some of the commenters. A broader definition of basis contract would result in the exclusion of more derivative contracts from the definition of referenced contract than previously proposed. A contract excluded from the definition of referenced contract is not subject to position limit under this Reproposal. The Commission declines to exclude more than the locational basis contracts that it previously proposed from the definition of referenced contract.

The Commission is reproposing Appendix B as originally proposed. The Commission is not persuaded by commenters' suggestions for expanding the current list of commodities considered ''substantially the same'' in Appendix B. While a commenter requested the Commission expand the list to address all ''commercial practices'' used by market participants, the Commission believes this request is too vague and too broad to be workable. In addition, although a commenter recommended that the Commission adopt a flexible process for identifying any additional commodities that are substantially the same as a commodity underlying a core referenced futures contract for inclusion in Appendix B,[278] the Commission observes that market participants are already provided the flexibility of two processes: (i) To request an exemptive, no-action or interpretative letter under § 140.99; and/or (ii) to petition for changes to Appendix B under § 13.2. Under either process, the Commission would need to carefully consider whether it would be beneficial and consistent with the policies underlying CEA section 4a to list additional commodities as substantially the same as a commodity underlying a core referenced futures contract, especially since various market participants might have conflicting views on such a determination in certain cases.

Finally, the Commission notes that comments regarding other types of differentials were addressed in the Commission's 2016 Supplemental Position Limits Proposal, which would allow exchanges to grant spread exemptions, including calendar spreads, quality differential spreads, processing spreads, and product or by-product differential spreads.[279] Comments responding to that 2016 Supplemental Position Limits Proposal and the Commission's Reproposal are discussed below.

b. Commodity Derivative Contract

*Proposed Rule:* The December 2013 Position Limits Proposal would define in § 150.1 the term ''commodity derivative contract'' for position limits purposes as shorthand for any futures, option, or swap contract in a commodity (other than a security futures product as defined in CEA section 1a(45)). The proposed use of such a generic term would be a convenient way to streamline and simplify references in part 150 to the various kinds of contracts to which the position limits regime applies. As such, this new definition can be found frequently throughout the Commission's proposed amendments to part 150.[280]

*Comments Received:* The Commission received no comments on the proposed definition.

*Commission Reproposal:* The Commission has determined to repropose the definition as proposed for the reasons given above.

c. Commodity Index Contract, Spread Contract, Calendar Spread Contract, and Intercommodity Spread Contract

*Proposed Rule:* The December 2013 Position Limits Proposal excluded commodity index contracts from the definition of referenced contracts; thus, commodity index contracts would not be subject to position limits. The Commission also proposed to define the term commodity index contract, which is not in current § 150.1, to mean ''an agreement, contract, or transaction that is not a basis contract or any type of spread contract, based on an index comprised of prices of commodities that are not the same or substantially the same.''

Further, the Commission proposed to add a definition of basis contract, as discussed above, and spread contract to clarify which types of contracts would not be considered a commodity index contract and thus would be subject to position limits. Under the proposal, a spread contract was defined as ''a calendar spread contract or an intercommodity spread contract.'' [281] Finally, the Commission proposed the addition of definitions for a calendar spread contract, and an intercommodity spread contract to clarify the meanings of those terms. In particular, under the proposal, a calendar spread contract would mean ''a cash-settled agreement, contract, or transaction that represents the difference between the settlement price in one or a series of contract months of an agreement, contract or transaction and the settlement price of another contract month or another series of contract months' settlement prices for the same agreement, contract or transaction.'' An intercommodity spread contract would mean ''a cash-settled agreement, contract or transaction that represents the difference between the settlement price of a referenced contract and the settlement price of another contract, agreement, or transaction that is based on a different commodity.'' [282]

The December 2013 Position Limits Proposal further noted that part 20 of the Commission's regulations requires reporting entities to report commodity reference price data sufficient to distinguish between commodity index contract and non-commodity index contract positions in covered contracts.[283] Therefore, for commodity index contracts, the Commission stated its intention to rely on the data elements in § 20.4(b) to distinguish data records subject to § 150.2 position limits from those contracts that are excluded from § 150.2. The Commission explained that this would enable the Commission to set position limits using the narrower data set (*i.e.,* referenced contracts subject to § 150.2 position limits) as well as conduct surveillance using the broader data set.[284]

*Comments Received:* The Commission received no comments on the proposed definitions for commodity index contract, spread contract, calendar spread contract, and intercommodity spread contract.[285]

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[278] As noted above, according to the commenter, a flexible process would allow market participants to request a timely interpretation regarding whether a particular commodity is substantially the same as a core referenced futures contract or that a particular contract qualifies as a ''basis contract. *See* CL–FIA–59595 at 19

[279] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38476–80.

[280] *See, e.g.,* amendments to § 150.1 (the definitions of: ''location basis contract,'' the definition of ''bona fide hedging position,'' ''inter-market spread position,'' ''intra-market spread position,'' ''pre-existing position,'' ''speculative position limits,'' and ''spot month''), §§ 150.2(f)(2), 150.3(d), 150.3(h), 150.5(a), 150.5(b), 150.5(e), 150.7(d), 150.7(f), Appendix A to part 150, and Appendix C to part 150.

[281] In the December 2013 Position Limits Proposal, the Commission noted that while the proposed definition of ''referenced contract'' specifically excluded guarantees of a swap, basis contracts and commodity index contracts, spread contracts were not excluded from the proposed definition of ''referenced contract.'' The December 2013 Position Limits Proposal at 75702.

[282] In the December 2013 Position Limits Proposal, the Commission also clarified that if a swap was based on the difference between two prices of two different commodities, with one linked to a core referenced futures contract price (and the other either not linked to the price of a core referenced futures contract or linked to the price of a different core referenced futures contract), then the swap was an ''intercommodity spread contract,'' was not a commodity index contract, and was a referenced contract subject to the position limits specified in § 150.2. The Commission further clarified that a contract based on the prices of a referenced contract and the same or substantially the same commodity (and not based on the difference between such prices) was not a commodity index contract and was a referenced contract subject to position limits specified in § 150.2. *See* December 2013 Position Limits Proposal, 78 FR at 75697, n. 163.

[283] *Id.* at 75697, n. 163.

[284] *Id.* at 75697.

[285] The Commission notes that although it did not receive comments on the proposed definitions for commodity index contract, spread contract, calendar spread contract, and intercommodity spread contract, it did receive a number of comments regarding the interplay of those defined terms and the definition of ''referenced contract.'' Discussion of those comments are included in the discussion of the proposed definition of ''referenced contract'' below.

*Commission Reproposal:* The Commission has determined to repropose the definitions as originally proposed for the reasons provided above, with the exception that, under the Reproposal, the term ''basis contract'' will be replaced with the term ''location basis contract,'' in the reproposed definition of commodity index contract, to conform to the name change discussed above. In addition, the Commission notes that while it had proposed to subsume the definitions of commodity index contract, spread contract, calendar spread contract, and intercommodity spread contract under the definition of referenced contract, in the Reproposal it is enumerating each as a separate definition for ease of reference.

d. Core referenced Futures Contract

*Proposed Rule:* The December 2013 Position Limits Proposal provided a list of futures contracts in § 150.2(d) to which proposed position limit rules would apply. The Commission proposed the term ''core referenced futures contract'' as a short-hand phrase to denote such contracts.[286] Accordingly, the Commission proposed to include in § 150.1 a definition of core referenced futures contract to mean ''a futures contract that is listed in § 150.2(d).'' In its proposal, the Commission also clarified that core referenced futures contracts include options that expire into outright positions in such contracts.[287]

*Comments Received:* The Commission received no comments on the proposed definition.

*Commission Reproposal:* The Commission has determined to repropose the definition as originally proposed.

e. Eligible Affiliate

*Proposed Rule:* The term ''eligible affiliate,'' used in proposed § 150.2(c)(2), is not defined in current § 150.1. The Commission proposed to amend § 150.1 to define an ''eligible affiliate'' as an entity with respect to which another person: (1) Directly or indirectly holds either: (i) A majority of the equity securities of such entity, or (ii) the right to receive upon dissolution of, or the contribution of, a majority of the capital of such entity; (2) reports its financial statements on a consolidated basis under Generally Accepted Accounting Principles or International Financial Reporting Standards, and such consolidated financial statements include the financial results of such entity; and (3) is required to aggregate the positions of such entity under § 150.4 and does not claim an exemption from aggregation for such entity.[288]

The definition of ''eligible affiliate'' proposed in the December 2013 Position Limits Proposal qualified persons as eligible affiliates based on requirements similar to those adopted by the Commission in a separate rulemaking.[289] On April 1, 2013, the Commission provided relief from the mandatory clearing requirement of CEA section 2(h)(1)(A) of the Act for certain affiliated persons if the affiliated persons (''eligible affiliate counterparties'') meet requirements contained in § 50.52.[290] Under both § 50.52 and the definition proposed in the December 2013 Position Limits Proposal, a person is an eligible affiliate if another person (*e.g.* a parent company), directly or indirectly, holds a majority ownership interest in such affiliates, reports its financial statements on a consolidated basis under Generally Accepted Accounting Principles or International Financial Reporting Standards, and such consolidated financial statements include the financial results of such affiliates. In addition, for purposes of the position limits regime, that other person (*e.g.,* a parent company) must be required to aggregate the positions of such affiliates under § 150.4 and not claim an exemption from aggregation for such affiliates.[291]

*Comments Received:* The Commission received few comments on the proposed definition of ''eligible affiliate.'' Commenters requested that the Commission harmonize the definition of ''eligible affiliate'' with the definition of ''eligible affiliate counterparty'' under § 50.52 in order to include ''sister affiliates'' within the definition.[292]

*Commission Reproposal:* The Commission notes that under § 150.4, aggregation is required by a person that holds an ownership or equity interest of 10 percent or greater in another person, unless an exemption applies. Under reproposed § 150.2(c)(2), sister affiliates would not be required to comply separately with position limits, provided such entities are eligible affiliates.[293]

As such, the Commission does not believe a there is a need to conform the ''eligible affiliate'' definition in reproposed § 150.1 to the definition of ''eligible affiliate counterparty'' in § 50.52 in order to accommodate sister affiliates. The Commission notes that a third person that holds an ownership or equity interest in each of the sister affiliates—*e.g.,* the parent company—would be required to aggregate positions of such eligible affiliates. Thus, the Commission is reproposing the definition without changes.

f. Entity

*Proposed Rule:* The December 2013 Position Limits Proposal defined ''entity'' to mean ''a 'person' as defined in section 1a of the Act.'' [294] The term, not defined in current § 150.1, is used in a number of contexts, and in various definitions in the proposed amendments to part 150. Thus, the definition originally proposed would provide a clear and unambiguous meaning for the term, and prevent confusion.

*Comments Received:* The Commission received no comments on the proposed definition.

*Commission Reproposal:* The Commission has determined to repropose the definition as originally proposed, for the reasons provided above.

g. Excluded Commodity

*Proposed Rule:* The phrase ''excluded commodity'' was added into the CEA in the CFMA, and is defined in CEA

[286] The selection of the core referenced futures contracts is explained in the discussion of § 150.2. *See* discussion below.

[287] *See* 78 FR at 75697 n. 166.

[288] *See* proposed § 150.1.

[289] *See* December 2013 Position Limits Proposal, 78 FR at 75698.

[290] *See* Clearing Exemption for Swaps Between Certain Affiliated Entities, 78 FR 21749, 21783, Apr. 11, 2013. Section 50.52(a) addresses eligible affiliate counterparty status, allowing a person not to clear a swap subject to the clearing requirement of section 2(h)(1)(A) of the Act and part 50 if the person meets the requirements of the conditions contained in paragraphs (a) and (b) of § 50.52. The conditions in paragraph (a) of § 50.52 specify either one counterparty holds a majority ownership interest in, and reports its financial statements on a consolidated basis with, the other counterparty, or both counterparties are majority owned by a third party who reports its financial statements on a consolidated basis with the counterparties.

The conditions in paragraph (b) of § 50.52 address factors such as the decision of the parties not to clear, the associated documentation, audit, and recordkeeping requirements, the policies and procedures that must be established, maintained, and followed by a dealer and major swap participant, and the requirement to have an appropriate centralized risk management program, rather than the nature of the affiliation. As such, those conditions are less pertinent to the definition of eligible affiliate.

[291] *See* December 2013 Position Limits Proposal, 78 FR at 75698; *see also* definition of ''eligible affiliate'' in § 150.1, as proposed therein.

[292] *See, e.g.,* CL–ISDA/SIFMA–59611 at 3 and 33, CL–Working Group–59693 at 66–7.

[293] Of course, sister affiliates would be required to aggregate, as would any other market participants, if they were trading together pursuant to an express or implied agreement.

[294] CEA section 1a(38); 7 U.S.C. 1a(38). *See also* December 2013 Position Limits Proposal, 78 FR at 75698.

section 1a(19), but is not defined or used in current part 150.[295] CEA section 4a(a)(2)(A), as amended by the Dodd-Frank Act, utilizes the phrase ''excluded commodity'' when it provides a timeline under which the Commission is charged with setting limits for futures and option contracts other than on excluded commodities.[296]

The December 2013 Position Limits Proposal included in § 150.1, a definition of excluded commodity that simply incorporates the statutory meaning, as a useful term for purposes of a number of the proposed changes to part 150. For example, the phrase was used in the proposed amendments to § 150.5, in its provision of requirements and acceptable practices for DCMs and SEFs in their adoption of rules and procedures for monitoring and enforcing position limits and accountability provisions; the phrase was also used in the definition of bona fide hedging position.

*Comments Received:* The Commission received no comments on the proposed definition.

*Commission Reproposal:* The Commission has determined to repropose the definition as previously proposed, for the reasons provided above.

h. First Delivery Month of the Crop Year

*Proposed Rule:* The term ''first delivery month of the crop year'' is currently defined in § 150.1(c), with a table of the first delivery month of the crop year for the commodities for which position limits are currently provided in § 150.2. The crop year definition had been pertinent for purposes of the spread exemption to the individual month limit in current § 150.3(a)(3), which limits spreads to those between individual months in the same crop year and to a level no more than that of the all-months limit.[297] Under the December 2013 Position Limits Proposal, the definition of ''crop year'' would be deleted from § 150.1. The proposed elimination of the definition conformed with level of individual month limits set at the level of the all-months limits, thus negating the purpose of the existing spread exemption in current § 150.3(a)(3), which the December 2013 Position Limits Proposal also eliminated.

The Commission notes that in its 2016 Supplemental Position Limits Proposal, the Commission proposed to retain a spread exemption in § 150.3 and not, as proposed in the December 2013 Position Limits Proposal, to eliminate it altogether.[298]

*Comments Received:* The Commission received no comments on the proposed deletion of the crop year definition.

*Commission Reproposal:* The Commission has determined to repropose the deletion of the definition of the term ''first delivery month of the crop year'' as originally proposed. The Commission notes that, although in its 2016 Supplemental Position Limits Proposal, the Commission proposed to retain a spread exemption in § 150.3 and, in fact, provides for the approval by exchanges of exemptions to spread positions beyond the limited exemption for spread positions in current § 150.3(a)(3), the crop year definition remains unnecessary since the level of individual month limits has been set at the level of the all-months limits.

i. Futures Equivalent

*Proposed Rule:* In the December 2013 Position Limits Proposal, the Commission proposed to broaden the definition of the term ''futures-equivalent'' found in current § 150.1(f) of the Commission's regulations,[299] and to expand upon clarifications included in the current definition relating to adjustments and computation times.[300] The Dodd-Frank Act amendments to CEA section 4a,[301] in part, direct the Commission to apply aggregate federal position limits to physical commodity futures contracts and to swaps contracts that are economically equivalent to such physical commodity futures contracts on which the Commission has established limits. In order to aggregate positions in futures, options and swaps contracts, it is necessary to adjust the position sizes, since such contracts may have varying units of trading (*e.g.,* the amount of a commodity underlying a particular swap contract could be larger than the amount of a commodity underlying a core referenced futures contract). The Commission proposed to adjust position sizes to an equivalent position based on the size of the unit of trading of the core referenced futures contract. Under the December 2013 Position Limits Proposal, the definition of ''futures equivalent'' in current § 150.1(f), which is applicable only to an option contract, would be extended to both options and swaps.

In the 2016 Supplemental Position Limits Proposal, the Commission proposed two further clarifications to the definition of the term ''futures-equivalent.'' First, the Commission proposed to address circumstances in which a referenced contract for which futures equivalents must be calculated is itself a futures contract. The Commission noted that this may occur, for example, when the referenced contract is a futures contract that is a mini-sized version of the core referenced futures contract (*e.g.,* the mini-corn and the corn futures contracts).[302] The Commission proposed to clarify in proposed § 150.1 that the term ''futures-equivalent'' includes a futures contract which has been converted to an economically equivalent amount of an open position in a core

[295] CEA section 1a(19); 7 U.S.C. 1a(19).

[296] CEA section 4a(2)(A); 7 U.S.C. 6a(2)(A).

[297] Prior to the adoption of Part 151, a single-month limit was set at a level that was lower than the all-months-combined limit. Operating in conjunction with the lower single-month limit level, as noted below, § 150.3(a)(3) provides a limited exemption for calendar spread positions to exceed that single-month limit, as long as the single month position (including calendar spread positions) is no greater than the level of the all-months-combined limit. In part 151, the Commission determined to set the single-month position limit levels in § 150.2 at the same level as the all-months-combined limits; in vacating part 151, the court retained the amendments to § 150.2, leaving the single-month limit at the same level as those of the all-months-combined limit levels. The December 2013 Position Limits Proposal retained parity of the single-month limit and all-months-combined limits levels.

[298] Moreover, the 2016 Supplemental Position Limits Proposal did not limit the exemption to spread positions held between individual months of a futures contract in the same crop year, nor limit the size of an individual month position to the all-months limit.

[299] 17 CFR 150.1(f) currently defines ''futures-equivalent'' only for an option contract, adjusting the open position in options by the previous day's risk factor, as calculated at the close of trading by the exchange.

[300] The December 2013 Position Limits Proposal defined ''futures-equivalent'' for: (1) An option contact, adjusting the position size by an economically reasonable and analytically supported risk factor, computed as of the previous day's close or the current day's close or contemporaneously during the trading day; and (2) a swap, converting the position size to an economically equivalent amount of an open position in a core referenced futures contract. *See* December 2013 Position Limits Proposal, 78 FR at 75698–9.

[301] Amendments to CEA section 4a(1) authorize the Commission to extend position limits beyond futures and option contracts to swaps traded on an exchange and swaps not traded on an exchange that perform or affect a significant price discovery function with respect to regulated entities. 7 U.S.C. 6a(a)(1). In addition, under new CEA sections 4a(a)(2) and 4a(a)(5), speculative position limits apply to agricultural and exempt commodity swaps that are ''economically equivalent'' to DCM futures and option contracts. 7 U.S.C. 6a(a)(2) and (5).

[302] Under current § 150.2, for purposes of compliance with federal position limits, positions in regular sized and mini-sized contracts are aggregated. The Commission's practice of aggregating futures contracts when a DCM lists for trading two or more futures contracts with substantially identical terms, is to scale down a position in the mini-sized contract, by multiplying the position in the mini-sized contract by the ratio of the unit of trading in the mini-sized contract to that of the regular sized contract. *See* paragraph (b)(2)(D) of app. C to part 38 of the Commission's regulations for guidance regarding the contract size or trading unit for a futures or futures option contract.

referenced futures contract. This clarification would mirror the expanded definition of ''futures-equivalent'' in the December 2013 Position Limits Proposal, as it would pertain to swaps.

Second, the Commission proposed in the 2016 Supplemental Position Limits Proposal to clarify the definition of the term ''futures-equivalent'' to provide that, for purposes of calculating futures equivalents, an option contract must also be converted to an economically equivalent amount of an open position in a core referenced futures contract. This clarification would address situations, for example, where the unit of trading underlying an option contract (that is, the notional quantity underlying an option contract) may differ from the unit of trading underlying a core referenced futures contract.[303]

The Commission expressed the view in the 2016 Supplemental Position Limits Proposal that these clarifications would be consistent with the methodology the Commission used to provide its analysis of unique persons over percentages of the proposed position limit levels in the December 2013 Position Limits Proposal.[304]

*Comments Received:* The Commission received two comments on the proposed definition of ''futures-equivalent'' in the December 2013 Position Limits Proposal.[305] Each comment was generally supportive of the proposed definition. Although one commenter commended the flexibility granted to market participants to use different option valuation models, it recommended that the Commission provide guidance on when it would consider an option valuation model unsatisfactory and what the factors the Commission would consider in arriving at such an opinion.[306] According to the commenter, the Commission should utilize a ''reasonableness approach'' by explicitly providing a ''safe harbor'' for models that produce results within 10 percent of an exchange or Commission model, and should permit market participants to demonstrate the reasonableness under prevailing market conditions of any model that falls outside this safe harbor.[307] It was also recommended that the Commission consider the exchanges' approach to option valuation where appropriate because these approaches are already in use and familiar to market participants.[308]

Both MFA and FIA supported the optional use of the prior day's delta to calculate a futures-equivalent position for purposes of speculative position limit compliance.[309] In addition, each requested that the Commission confirm or adopt a provision similar to CME Rule 562. That exchange rule provides, among other things, that if a participant's position exceeds position limits as a result of an option assignment, that participant is allowed one business day to liquidate the excess position without being considered in violation of the limits. FIA urged the Commission to provide market participants with a reasonable period of time to reduce its position below the speculative position limit.[310]

*Commission Reproposal:* The Commission has determined to repropose the definition of ''futures-equivalent'' as proposed in the 2016 Supplemental Position Limits proposal, with the exception that it now proposes adopting the current exchange practice with regard to option assignments, as discussed below.

Regarding risk (delta) models, the Reproposal does not provide a ''safe harbor'' as requested since risk models, generally, should produce similar results. The Commission believes a difference of 10 percent above or below the delta resulting from an exchange's model generally would be too great to be economically reasonable. However, the Commission notes that, under the Reproposal, should a market participant believe its model produces an economically reasonable and analytically supported risk factor for a particular trading session that differs significantly from a result published by an exchange for that same time,[311] it may describe the circumstances that result in a significant difference and request that staff review that model for reasonableness.[312]

Regarding the time period for a participant to come into compliance because of option assignment, the Commission agrees that a participant in compliance only because of a previous day's delta, and no longer, after option assignment, in compliance on a subsequent day, should have one business day to liquidate the excess position resulting from option assignment without being considered in violation of the limits.[313] Exchanges currently provide the same amount of time to come into compliance.

j. Intermarket Spread Position and Intramarket Spread Position

*Proposed Rule:* In the December 2013 Position Limits Proposal, the Commission proposed to add to current § 150.1 new definitions of the terms ''intermarket spread position'' and ''intramarket spread position.'' [314] These terms were defined in the December 2013 Position Limits Proposal within the definition of ''referenced contract.'' In connection with its 2016 Supplemental Position Limits Proposal to permit exchanges to process applications for exemptions from federal position limits for certain spread positions, the Commission proposed to expand the definitions of these terms as proposed in the December 2013 Position Limits Proposal.

In particular, in the 2016 Supplemental Position Limits Proposal,

[303] For an example of a futures-equivalent conversion of a swaption, *see* example 6, WTI swaptions, Appendix A to part 20 of the Commission's regulations.

[304] 2016 Supplemental Position Limits Proposal, 81 FR at 38483. *See also* Table 11 in the December 2013 Position Limits Proposal, 78 FR at 75731–3.

[305] CL–MFA–59606; CL–FIA–59595 at 15.

[306] CL–MFA–59606 at 16–17.

[307] MFA also stated that the Commission should not second guess the results of reasonable models and impose findings of violations after-the-fact as that would introduce tremendous uncertainty into compliance with the position limits regime. *Id* at 17.

[308] *Id* at 17.

[309] CL–MFA–59606 at 17; CL–FIA–59595 at 15.

[310] CL–FIA–59595 at 15.

[311] Under § 16.01(a)(2), a reporting market is required to record for each trading session the option delta, when a delta system is used, while § 16.01(e) requires a reporting market to make that option delta readily available to the public. A reporting market for this purpose is defined in § 15.00(q) as a DCM or a registered entity under CEA section 1a(40) (under CEA section 1a(40), registered entities include, among others, DCMs, DCOs, SEFs, SDRs).

[312] Deltas are computed using an option pricing model. Different option pricing models incorporate different assumptions. For a discussion of circumstances where assumptions in an option pricing model may not hold, *see,* for example, Paul Wilmott, *Derivatives: The Theory and Practice of Financial Engineering* chapter 29 (1998) (describing circumstances where delta hedging an option position (*i.e.,* replication trading) can move the price of the underlying asset, violating an assumption of certain option pricing models that replication trading has no influence on the price of the underlying asset).

[313] The Commission believes that, in the circumstance of option assignment, one business day is a reasonable amount of time to come into compliance because the markets for commodities subject to federal limits under § 150.2 are generally liquid.

[314] In the December 2013 Position Limits Proposal, the Commission proposed to define an ''intermarket spread position'' as ''a long position in a commodity derivative contract in a particular commodity at a particular designated contract market or swap execution facility and a short position in another commodity derivative contract in that same commodity away from that particular designated contract market or swap execution facility.'' The Commission also proposed to define an ''intramarket spread position'' as ''a long position in a commodity derivative contract in a particular commodity and a short position in another commodity contract in the same commodity on the same designated contract market or swap execution facility.'' *See* December 2013 Position Limits Proposal, 78 FR at 75699–700.

the Commission proposed to define an ''intermarket spread position'' to mean ''a long (short) position in one or more commodity derivative contracts in a particular commodity, or its products or its by-products, at a particular designated contract market, and a short (long) position in one or more commodity derivative contracts in that same, or similar, commodity, or its products or its by-products, away from that particular designated contract market.'' Similarly, the Commission proposed in the 2016 Supplemental Position Limits Proposal to define an ''intramarket spread position'' to mean ''a long position in one or more commodity derivative contracts in a particular commodity, or its products or its by-products, and a short position in one or more commodity derivative contracts in the same, or similar, commodity, or its products or its by-products, on the same designated contract market.''

The Commission expressed the view that the expanded definitions proposed in the 2016 Supplemental Position Limits Proposal would take into account that a market participant may take positions in multiple commodity derivative contracts to establish an intermarket spread position or an intramarket spread position. The expanded definitions would also take into account that such spread positions may be established by taking positions in derivative contracts in the same commodity, in similar commodities, or in the products or by-products of the same or similar commodities. By way of example, the Commission noted that the expanded definitions would include a short position in a crude oil derivative contract and long positions in a gasoline derivative contract and a diesel fuel derivative contract (collectively, a reverse crack spread).

*Comments Received:* The Commission did not receive any comments in response to the definitions of ''intermarket spread position'' and ''intramarket spread position'' proposed in the December 2013 Position Limits Proposal [315] or in response to the 2016 Supplemental Position Limits Proposal.

*Commission Reproposal:* The Commission has determined to repropose the definitions of the terms ''intermarket spread position'' and ''intramarket spread position'' as proposed in the 2016 Supplemental Position Limits Proposal.

k. Long Position

*Proposed Rule:* The term ''long position'' is currently defined in § 150.1(g) to mean ''a long call option, a short put option or a long underlying futures contract.'' The Commission proposed to update the definition to make it also applicable to swaps such that a long position would include a long futures-equivalent swap.

*Commission Reproposal:* Though no commenters suggested changes to the definition of ''long position,'' the Commission is concerned that the proposed definition does not clearly articulate that futures and options contracts are subject to position limits on a futures-equivalent basis in terms of the core referenced futures contract. Longstanding market practice has applied position limits on futures and options on a futures-equivalent basis, and the Commission believes that practice ought to be made explicit in the definition in order to prevent confusion. Thus, the Commission is reproposing an amended definition to clarify that a long position is ''on a futures-equivalent basis, a long call option, a short put option, a long underlying futures contract, or a swap position that is equivalent to a long futures contract.'' This clarification is consistent with the clarification to the definition of futures-equivalent basis proposed in the 2016 Supplemental Position Limits Proposal. Though the substance of the definition is fundamentally unchanged, the revised language should prevent unnecessary confusion over the application of futures-equivalency to different kinds of commodity derivative contracts.

l. Physical Commodity

*Proposed Rule:* The December 2013 Position Limits Proposal would amend § 150.1 by adding in a definition of the term ''physical commodity'' for position limit purposes. Congress used the term ''physical commodity'' in CEA sections 4a(a)(2)(A) and 4a(a)(2)(B) to mean commodities ''other than excluded commodities as defined by the Commission.'' Therefore, the Commission interprets ''physical commodities'' to include both exempt and agricultural commodities, but not excluded commodities, and proposes to define the term as such.[316]

*Comments Received:* The Commission received no comments on the proposed definition.

*Commission Reproposal:* The Commission has determined to repropose the definition as originally proposed.

m. Pre-enactment Swap and Pre-Existing Position

*Proposed Rule:* The December 2013 Position Limits Proposal would amend § 150.1 by adding in new definitions of the terms ''pre-enactment swap'' and ''pre-existing position'' for position limit purposes. Under the definitions proposed in the December 2013 Position Limits Proposal, ''pre-enactment swap'' means any swap entered into prior to enactment of the Dodd-Frank Act of 2010 (July 21, 2010), the terms of which have not expired as of the date of enactment of that Act, while ''pre-existing position'' means any position in a commodity derivative contract acquired in good faith prior to the effective date of any bylaw, rule, regulation or resolution that specifies an initial speculative position limit level or a subsequent change to that level.

*Comments Received:* The Commission received no comments on the proposed definitions either of the terms ''pre-enactment swap'' or ''pre-existing position.''

*Commission Reproposal:* The Commission has determined to repropose both definitions as previously proposed.

n. Referenced Contract

*Proposed Rule:* Part 150 currently does not include a definition of the phrase ''referenced contract,'' which was introduced and adopted in vacated part 151.[317] As was noted when part 151 was adopted, the Commission identified 28 core referenced futures contracts and proposed to apply aggregate limits on a futures equivalent basis across all derivatives that met the definition of referenced contracts.[318] The definition of referenced contract proposed in the December 2013 Position Limits Proposal was similar to that of vacated part 151,

[315] As noted above, the definitions of ''intermarket spread position'' and ''intramarket spread position'' were included.

[316] For position limits purposes, proposed § 150.1 would define ''physical commodity'' to mean any agricultural commodity as that term is defined in § 1.3 of this chapter or any exempt commodity as that term is defined in section 1a(20) of the Act.

[317] Vacated § 151.1 defined ''Referenced Contract'' to mean ''on a futures-equivalent basis with respect to a particular Core Referenced Futures Contract, a Core Referenced Futures Contract listed in § 151.2, or a futures contract, options contract, swap or swaption, other than a basis contract or contract on a commodity index that is: (1) Directly or indirectly linked, including being partially or fully settled on, or priced at a fixed differential to, the price of that particular Core Referenced Futures Contract; or (2) directly or indirectly linked, including being partially or fully settled on, or priced at a fixed differential to, the price of the same commodity underlying that particular Core Referenced Futures Contract for delivery at the same location or locations as specified in that particular Core Referenced Futures Contract.''

[318] Position Limits for Futures and Swaps, 76 FR at 71629.

but there were certain differences, including an exclusion of guarantees of swaps and the incorporation of other terms into the definition of referenced contract.

In the December 2013 Position Limits Proposal, the term ''referenced contract'' was proposed to be defined in § 150.1 to mean, on a futures-equivalent basis with respect to a particular core referenced futures contract, a core referenced futures contract listed in § 150.2(d) of this part, or a futures contract, options contract, or swap, other than a guarantee of a swap, a basis contract, or a commodity index contract: (1) That is: (a) Directly or indirectly linked, including being partially or fully settled on, or priced at a fixed differential to, the price of that particular core referenced futures contract; or (b) directly or indirectly linked, including being partially or fully settled on, or priced at a fixed differential to, the price of the same commodity underlying that particular core referenced futures contract for delivery at the same location or locations as specified in that particular core referenced futures contract; and (2) where: (a) Calendar spread contract means a cash-settled agreement, contract, or transaction that represents the difference between the settlement price in one or a series of contract months of an agreement, contract or transaction and the settlement price of another contract month or another series of contract months' settlement prices for the same agreement, contract or transaction; (b) commodity index contract means an agreement, contract, or transaction that is not a basis or any type of spread contract, based on an index comprised of prices of commodities that are not the same or substantially the same; (c) spread contract means either a calendar spread contract or an intercommodity spread contract; and (d) intercommodity spread contract means a cash-settled agreement, contract or transaction that represents the difference between the settlement price of a referenced contract and the settlement price of another contract, agreement, or transaction that is based on a different commodity.

*Comments Received:* The Commission received numerous comments [319] regarding various aspects of the definition of ''referenced contract.'' Some were generally supportive of the proposed definition while others suggested changes. One commenter expressly stated its support for speculative limits on futures, options, and swaps because each financial instrument ''can be used to develop market power and increase volatility.'' [320] Another commenter expressed its support for the exclusion of guarantees of swaps from the definition of referenced contract.[321] These comments and the Commission's response are detailed below.

*Commission Reproposal:* The Commission is reproposing the definition of referenced contract with two substantive modifications from the original proposal, both of which are discussed further below. First, the Commission is now proposing to amend the definition of ''referenced contract'' to expressly exclude trade options. Second, the Reproposal would clarify the meaning of ''indirectly linked.'' The Reproposal also moves four definitions that were embedded in the proposed definition of referenced contract, specifically ''calendar spread contract,'' ''commodity index contract,'' ''spread contract,'' and ''intercommodity spread contract,'' to their own definitions in § 150.1, while otherwise retaining those definitions as proposed. In addition, the Reproposal makes non-substantive modifications to the definition of referenced contract to make it easier to read.

*Comments Received:* In response to a specific request for comment in the December 2013 Position Limits Proposal, many commenters recommended excluding trade options from the definition of referenced contract.[322]

*Commission Reproposal:* In response to numerous comments, the reproposed definition of ''referenced contract'' expressly excludes trade options that meet the requirements of § 32.3. The Commission notes that in its trade options final rule,[323] the cross-reference to vacated part 151 position limits was deleted from § 32.3(c). At that time, the Commission stated its belief that federal speculative position limits should not apply to trade options, as well as its intention to address trade options in the context of the any final rulemaking on position limits.[324] Therefore, the Commission is reproposing the definition of ''referenced contract'' to expressly exclude trade options that meet the requirements of § 32.3 of this chapter.

*Comments Received:* Commenters asserted that certain aspects of the definition of referenced contract are unclear and/or unworkable. For example, commenters suggested that the concept of ''indirectly linked'' is unclear and so market participants may not know whether a particular contract is subject to limits.[325] Some commenters believe that the definition is overbroad and captures products that they state do not affect price discovery or impair hedging and are not truly economically-equivalent.[326] Commenters request that the Commission support its determination regarding which contracts are economically equivalent by providing a description of the methodology used to determine the contracts considered to be economically-equivalent, including examples of over-the-counter (''OTC'') and FBOT contracts.[327] One commenter stated that support is necessary because ''mechanically assign[ing]'' the label of economically-equivalent to any contract that references a core referenced futures contract does not make it equivalent.[328]

*Commission Reproposal:* The Commission agrees with commenters that there is a need to clarify the meaning of ''indirectly linked.'' The Commission notes that including contracts that are ''indirectly linked'' to the core referenced futures contract under the definition of referenced contract is intended to prevent the evasion of position limits through the creation of an economically equivalent contract that does not directly reference the core referenced futures contract price. Under the reproposed definition, ''indirectly linked'' means a contract that settles to a price based on another derivative contract that, either directly or through linkage to another derivative contract, has a settlement price based on

[319] The commenters included AGA, APGA, Atmos, API, Better Markets, BG Group, Calpine, Citadel, CME, CMOC, COPE, DEU, EEI, EPSA, FIA, ICE, IECA, ISDA/SIFMA, GFMA, IATP, MFA, NEM, NFP, NGSA, OLAM, PAAP, SCS, and Vectra.

[320] CL–IECA–59713 at 4.

[321] CL–IECAssn–59679 at 31.

[322] *See, e.g.,* CL–FIA–59595 at 4 and 19, CL–EEI–EPSA–59602 at 3, CL–ISDA/SIFMA–59611 at 3 and 34, CL–NEM–59620 at 2, CL–DEU–59627 at 7, CL–AGA–59632 at 4–5, CL–AGA–60382 at 10, CL–Olam–59658 at 3, CL–BG Group–59656 at 4, CL–BG Group–60383 at 4, CL–COPE–59662 at 5 and 8, CL–Calpine–59663 at 5, CL–PAAP–59664 at 4, CL–NGSA–59673 at 27–33, CL–ICE–59669 at 13, CL–EPSA–60381 at 4–5, CL–A4A–59714 at 5, CL–NFP–59690 at 7–8, CL–Working Group–59693 at 55–58, CL–API–59694 at 7, CL–IECAssn–59679 at 22, CL–IECAssn–59957 at 6–9, CL–Atmos–59705 at 4, CL–APGA–59722 at 9, CL–EEI–59945 at 5–6, CL–EPSA–55953 at 6–7, and CL–SCS–60399 at 3.

[323] Trade Options, 81 FR 14966 (Mar. 21, 2016).

[324] *Id.* at 14971.

[325] *See, e.g.,* CL–CMC–59634 at 14, and CL–COPE–59662 at 7, n. 20 (stating ''[i]t is one thing if the Commission means a reference to a contract that itself directly references a core referenced futures contract. It is more troubling and likely unworkable if the Commission means a more subjective economic link to a delivery location that is used in a core referenced futures contract. At a minimum, the Commission should provide examples of indirect linkage that triggers referenced contract status'').

[326] *See, e.g.,* CL–COPE–59662 at 7, and CL–BG Group–59656 at 4.

[327] *See, e.g.,* CL–MFA–59606 at 4 and 15–16.

[328] CL–COPE–59950 at 7.

the price of a core referenced futures contract or based on the price of the same commodity underlying that particular core referenced futures contract for delivery at the same location specified in that particular core referenced futures contract. Therefore, contracts that settle to the price of a referenced contract, for example, would be indirectly linked to the core referenced futures contract (*e.g.,* a swap that prices to the ICE Futures US Henry LD1 Fixed Price Futures (H) contract, which is a referenced contract that settles directly to the price of the NYMEX Henry Hub Natural Gas (NG) core referenced futures contract).

On the other hand, an outright derivative contract whose settlement price is based on an index published by a price reporting agency (''PRA'') that surveys cash market transaction prices (even if the cash market practice is to price at a differential to a futures contract) would not be directly or indirectly linked to the core referenced futures contract.[329] Similarly, a derivative contract whose settlement price was based on the same underlying commodity at a different delivery location (*e.g.,* ultra-low sulfur diesel delivered at L.A. Harbor) would not be linked, directly or indirectly, to the core referenced futures contract. The Commission is publishing an updated *CFTC Staff Workbook of Commodity Derivative Contracts Under the Regulations Regarding Position Limits for Derivatives* along with this release, which provides a non-exhaustive list of referenced contracts and may be helpful to market participants in determining categories of contracts that fit within the definition. Under the Reproposal, as always, market participants may request clarification from the Commission when necessary.

Regarding comments that the definition is overbroad and captures products that commenters state do not affect price discovery or are not truly economically-equivalent, the Commission notes that commenters seem to be confusing the statutory definitions of ''significant price discovery function'' (in CEA section 4a(a)(4)) and ''economically equivalent'' (in CEA section 4a(a)(5)). As a matter of course, contracts can be economically equivalent without serving a significant price discovery function. The Commission notes that there is no unpublished methodology used to determine which contracts are referenced contracts. Instead, the Commission proposed, and, following notice and comment, is now reproposing a definition for referenced contracts, and contracts that fit under that definition will be subject to federal speculative position limits.

*Comments Received:* Several commenters suggested that cash-settled contracts should not be subject to position limits.[330] One commenter asserted that non-deliverable cash-settled contracts are ''fundamentally different'' from deliverable commodity contracts and should not be subject to position limits.[331] The commenter also asserted that subjecting penultimate-day contracts such as options to a limit structure would make managing an option portfolio ''virtually impossible'' and would result in confusion and uncertainty.[332]

*Commission Reproposal:* The Commission has determined not to make any changes in the Reproposal that would broadly exempt cash-settled contracts from position limits. Cash-settled contracts are economically equivalent to deliverable contracts, and Congress has required that the Commission impose limits on economically equivalent swaps. The Commission notes that Congress took action twice to address this issue. In CEA section 4a(a)(5)(A), Congress required the Commission to adopt position limits for swaps that are economically equivalent to futures or options on futures or commodities traded on a futures exchange, for which the Commission has adopted position limits. Previously, in the CFTC Reauthorization Act of 2008,[333] Congress imposed a core principle for position limitations on swaps that are significant price discovery contracts.[334] In addition, because cash-settled referenced contracts are economically equivalent to the physical delivery contract in the same commodity, a trader has an incentive to manipulate one contract in order to benefit the other.[335] The Commission notes that a trader with positions in both the physically delivered and cash-settled referenced contracts would have, in the absence of position limits, increased ability to manipulate one contract to benefit positions in the other.

Moreover, if speculators were incentivized to abandon physical delivery contracts for cash-settled contracts so as to avoid position limits, it could result in degradation of the physical delivery contract markets that position limits are intended and designed to protect.

*Comments Received:* One commenter asked the Commission to confirm that a non-transferable repurchase right granted in connection with a hedged commodity transaction does not count towards position limits, citing CME Group and ICE Futures rules to that effect. The commenter is concerned that such a transaction could be deemed a commodity option and therefore legally a swap, but that it believed the transaction satisfies the criteria for exemption from definition as a swap.[336]

*Commission Reproposal:* As the commenter notes, whether the contract is subject to position limits depends on whether it is a swap. The Commission points out that the release adopting the definition of swap noted the Commission's belief that its forward contract interpretation ''provides sufficient clarity with respect to the forward contract exclusion from the swap and future delivery definitions.'' [337] Also in that release, the Commission noted that commodity options are swaps.[338] Separately, the Commission adopted Commission § 32.3, providing an exemption from the commodity option definition for trade options; the exemption was recently further amended.[339] The commenter should apply these rules to determine whether a given contract is a swap. In addition, the Commission notes that under Commission § 140.99, the commenter may request clarification or exemptive relief regarding whether a non-transferable repurchase right falls under the definition of a ''swap.'' To the extent the commenter seeks a clarification or change to the definition of a swap, the current rulemaking has not been expanded to revisit that definition.

[329] The Commission notes that while the outright derivative contract would not be indirectly linked to the core referenced contract, a derivative contract that settles to the difference between the core referenced futures contract and the PRA index would be directly linked because it settles in part to the core referenced futures contract price.

[330] *See, e.g.,* CL–Vectra–60369 at 3, and CL–Citadel–59717 at 9.

[331] CL–Vectra–60369 at 3.

[332] *Id.*

[333] Incorporated as Title XIII of the Food, Conservation and Energy Act of 2008, Pub. L. 110–246, 122 Stat. 1624 (June 18, 2008),

[334] CEA section 2(h)(7) (2009).

[335] Under the reproposed definition, a cash-settled contract must be linked, directly or indirectly, to the core referenced futures contract or the same underlying commodity in the same delivery location in order to be considered a ''referenced contract.''

[336] CL–Olam–59658 at 8–9.

[337] *See,* Further Definition of ''Swap,'' ''Security-Based Swap,'' and ''Security-Based Swap Agreement''; Mixed Swaps; Security-Based Swap Agreement Recordkeeping; Final Rule (''Swap Definition Rulemaking''), 77 FR 48208, 48231 (Aug. 13, 2012).

[338] *Id.* at 48237.

[339] *See* Commodity Options, 77 FR 25320, 75326 (Apr. 27, 2012); *see also* Trade Options, 81 FR 14966 (Mar. 21, 2016).

*Comments Received:* One commenter [340] requested clarification that a bid, offer, or indication of interest for an OTC swap that does not constitute a binding transaction will not count towards position limits, noting that current CME Rule 562 provides that such bids or offers would be in violation of the limit.

*Commission Reproposal:* The Reproposal does not change the definition originally proposed in response to the comment requesting clarification that a bid, offer, or indication of interest for an OTC swap that does not constitute a binding transaction will not count towards position limits. Nevertheless, the Commission clarifies that under the Reproposal, such bids, offers, or indications of interest do not count toward position limits.[341]

*Comments Received:* One commenter requested that the Commission exclude from the definition of referenced contract any agreement, contract, and transaction exempted from swap regulations by virtue of an exemption order, interpretation, no-action letter, or other guidance; the commenter stated that it believes the Commission can use its surveillance capacity and anti-manipulation authority, along with its MOU with FERC, to monitor these nonfinancial commodity transactions as well as the market participants relying on the exemptive relief.[342]

*Commission Reproposal:* The Reproposal does not change the proposed definition in response to the comment requesting that the Commission exclude from the definition of referenced contract any agreement, contract, and transaction exempted from swap regulations by virtue of an exemption order, interpretation, no-action letter, or other guidance. The Commission notes that any contract that is not a commodity derivative contract, including one that has been excluded from the definition of swap, is not subject to position limits. The commenter is requesting a broad exclusion from the definition of referenced contract, based on other regulatory relief which may have been adopted for a variety of policy reasons unrelated to position limits. Consequently, in light of the many and varied policy reasons for issuing an exemption order, interpretation, no-action letter or other guidance from swap regulation, each such action would need to be considered in the context of the goals of the Commission's position limits regime. Rather than issuing a blanket exemption from the definition of referenced contract for any agreement, contract, and transaction exempted from swap regulations, therefore, the Commission believes it would be better to consider each such action on its own merits prior to issuing an exemption from position limits. Under the Reproposal, if a market participant desires to extend a previously taken exemptive action by exempting certain agreements, contracts, and transactions from the definition of referenced contract, the market participant can request that the particular exemption order, interpretation, no-action letter, or other guidance be so extended. This would allow the Commission to consider the particular action taken and the merits of that particular exemption in the context of the position limits regime.

The Commission notes that in the particular exemptive order cited by the commenter,[343] certain delineated non-financial energy transactions between certain specifically defined entities were exempted, pursuant to CEA sections 4(c)(1) and 4(c)(6), from all requirements of the CEA and Commission regulations issued thereunder, subject to certain anti-fraud, anti-manipulation, and record inspection conditions. All entities that meet the requirements for the exemption provided by the Federal Power Act 201(f) Order are, therefore, already exempt from position limits compliance for all transactions that meet the Order's conditions.

*Comments Received:* Commenters were divided with respect to the exclusion of ''commodity index contracts'' from the definition of referenced contract. As a result of the exclusion, the position of a market participant who enters into a commodity index contract with a dealer will not be subject to position limits. One commenter supported the exclusion of commodity index contracts from the definition of referenced contracts.[344] The commenter was concerned, however, that a dealer who offsets his or her exposure in such contracts by purchasing futures contracts on the constituent components of the commodity index will be subject to position limits in the referenced contracts. The commenter urged the Commission to recognize as a bona fide hedge ''the offsetting nature of the dealer's position by exempting the futures contracts that a dealer acquires to hedge its commitments under commodity index contracts.'' [345] Alternatively, the Commission should ''modify the definition of 'referenced contract' and the definition of 'commodity derivative contract' by excluding core referenced futures contracts and related futures contracts, options contracts or swaps that are offset on an economically equivalent basis by the constituent portions of commodity index contracts.'' [346] Another commenter supported the Commission's proposal to exclude swaps that reference indices such as the Goldman Sachs Commodity Index (GSCI) from the definition of a referenced contract.[347]

One commenter asked that the Commission reconsider excluding commodity index contracts from the definition of referenced contract.[348] Another commenter urged that commodity index contracts should be included in the definition of referenced contract in conjunction with (1) a class limit (as was proposed for vacated part 151, but not included in final part 151); and (2) a lower position limit set at a level ''aimed to maintain no more than'' 30 percent speculation in each commodity (based on COT report classifications) that is reset every 6 months.[349] The same commenter noted that trading by passive, long only

[340] *See, e.g.,* CL–MFA–59606 at 5 and 23.

[341] The Commission notes that it is discussing bids, offers, and indications of interest in the context of whether these would violate position limits, and is not addressing other issues such as whether or not their use may indicate spoofing in violation of CEA section 4(c)(a)(5).

[342] CL–NFP–59690 at 14–15.

[343] *See* the Between NFP Electrics Exemptive Order (Order Exempting, Pursuant to Authority of the Commodity Exchange Act, Certain Transactions Between Entities Described in the Federal Power Act, and Other Electric Cooperatives, 78 FR 19670 (Apr. 2, 2013) (''Federal Power Act 201(f) Order''). *See also* CL–NFP–59690 at 14–15. The Federal Power Act 201(f) Order exempted all ''Exempt Non-Financial Energy Transactions'' (as defined in the Federal Power Act 201(f) Order) that are entered into solely between ''Exempt Entities'' (also as defined in the Federal Power Act 201(f) Order, namely any electric facility or utility that is wholly owned by a government entity as described in the Federal Power Act ('FPA') section 201(f); (ii) any electric facility or utility that is wholly owned by an Indian tribe recognized by the U.S. government pursuant to section 104 of the Act of November 2, 1994; (iii) any electric facility or utility that is wholly owned by a cooperative, regardless of such cooperative's status pursuant to FPA section 201(f), so long as the cooperative is treated as such under Internal Revenue Code section 501(c)(12) or 1381(a)(2)(C), and exists for the primary purpose of providing electric energy service to its member/owner customers at cost; or (iv) any other entity that is wholly owned, directly or indirectly, by any one or more of the foregoing.). *See* Federal Power Act 201(f) Order at 19688.

[344] CL–GFMA–60314 at 4.

[345] *Id.*

[346] *Id.*

[347] CL–CMOC–59720 at 4.

[348] CL–IATP–59701 at 2.

[349] CL–Better Markets–59716 at 1–35, and particularly at 32.

commodity index fund speculators does not provide liquidity, but rather takes net liquidity, dilutes the pool of market information to be less reflective of fundamental forces, causes volatility, and causes an increased frequency of contango attributed to frequent rolls from selling a nearby contract and buying a deferred (second month) contract. The commenter noted that, broadly, speculators in commodity futures historically constituted between 15 and 30 percent of open interest without meaningfully disrupting the market and providing beneficial intermediation between hedging producers and hedging consumers.[350]

*Commission Reproposal:* The Commission is reproposing the provision excluding commodity index contracts from the definition of referenced contract as previously proposed.

Regarding commenters who requested that the Commission alter the proposed definition to include commodity index derivative contracts, the Commission notes that if it were to include such contracts, the Commission's rules would allow netting of such positions in commodity index contracts with other offsetting referenced contracts. The ability to net such commodity index derivative contracts positions with other offsetting referenced contracts would eliminate the need for a bona fide hedging exemption for such contracts. Thus, the Commission believes such netting would contravene Congressional intent, as expressed in CEA section 4a(c)(B)(i) in its requirement to permit a pass-thru swap offset only if the counterparty's position would qualify as a bona fide hedge.

Another commenter suggested including commodity index contracts under the definition of referenced contract in conjunction with a class limit (*e.g.,* a separate limit for commodity index contracts compared to all other categories of derivative contracts). The commenter suggested that the limit be set at a level aimed at maintaining a particular ratio of speculative trading in the market. In response to this commenter, the Commission declines in this Reproposal to propose class limits because it believes any adoption of a class limit would require a rationing scheme wherein unrelated legal entities would be limited by the positions of other unrelated legal entities. Further, the Commission is concerned that class limits (including the one proposed by the commenter) could impair liquidity in the relevant markets.[351] The Commission also notes that it currently does not collect information to effectively enforce any ratio of speculative trading, and has not done so since the Commission eliminated Series '03 reporting in 1981.[352] The Reproposal does not make any changes to the definition of referenced contract pursuant to this comment.

Finally, in response to the commenter who suggested that, in addition to excluding commodity index contracts as proposed, the Commission should recognize as bona fide hedge positions those positions that offset a position in a commodity index derivative contract by using the component futures contracts, the Commission observes that it still believes, as discussed in the December 2013 Position Limits Proposal, that financial products do not meet the temporary substitute test. As such, the offset of financial risks arising from financial products is inconsistent with the statutory definition of a bona fide hedging position. The Commission also declines in this Reproposal to accept the commenter's request to exempt these offsetting positions using its authority under CEA section 4a(a)(7) because it does not believe that permitting the offset of financial risks furthers the purposes of the Commission's position limits regime as described in CEA section 4a(a)(3)(B). Finally, the commenter suggested as an alternative that the Commission modify the definition of referenced contract to broadly exclude any derivative contracts that are used to offset commodity index exposure. However, the Commission believes such a broad exclusion would, at best, be too difficult to administer and, at worst, provide an easy vehicle for entities to evade position limits regulations.

*Comments Received:* One commenter suggested that the Commission unnecessarily limited the scope of permissible netting by not recognizing cross-commodity netting, recommending either a threshold correlation factor of 60 percent or an approach that would permit pro rata netting to the extent of demonstrated correlation.[353]

*Commission Reproposal:* The Commission believes that recognizing cross-commodity netting as requested by the commenter would substantially expand the definition of referenced contract and, thus, may weaken: (1) The protection of the price discovery function in the core referenced futures contract; (2) the prevention of excessive speculation; and (3) the prevention of market manipulation. Therefore, this Reproposal does not change the definition of referenced contract to accommodate cross-commodity netting.

*Comments Received:* One commenter requested that all ''nonfinancial commodity derivatives'' used by commercial end-users for hedging purposes be expressly excluded from the definition of referenced contract (and so excluded from position limits). The commenter also suggested that the Commission allow an end-user to identify a swap as being used to ''hedge or mitigate commercial risks'' at the time the swap is executed and noted that such trades are highly-customized bilateral agreements that are difficult to convert into futures equivalents.[354] The commenter also requested that ''customary commercial agreements'' be excluded from referenced contract definition. The commenter stated that these contracts may reference a core referenced futures contract or may be misinterpreted as directly or indirectly linking to a core referenced futures contract, but that the Commission has already determined that Congress did not intend to regulate such agreements as swaps.[355]

*Commission Reproposal:* This Reproposal does not amend the definition of referenced contract in response to the request that ''nonfinancial commodity derivatives'' used by commercial end-users for hedging purposes be expressly excluded from the definition of referenced contract. The Commission understands the comment to mean that when a particular transaction qualifies for the end-user exemption, it should also be exempt from position limits by excluding such transactions from the definition of ''referenced contract.'' The commenter quotes language from the end-user exemption definition, which was issued to provide relief from the clearing and trade execution mandates. The Commission notes that under the CEA's statutory language, the commercial end user exemption

[350] CL–Better Markets–59716 at 5, and CL–Better Markets–60401 at 4, 16–17.

[351] *See also,* December 2013 Position Limits Proposal, 78 FR at 75741.

[352] The Commission's Series '03 reports required large traders to classify how much of their position was speculative and how much was hedging and formed the basis of the earliest versions of the CFTC Commitments of Traders Reports. *See* ''Reporting Requirements for Contract Markets, Futures Commission Merchants, Members of Exchanges and Large Traders,'' 46 FR 59960 (Dec. 8, 1981) (eliminating the routine of Series '03 reports by large traders).

[353] CL–ISDA/SIFMA–59611 at 3 and 32–33.

[354] CL–NFP–59690 at 9–12.

[355] CL–NFP–59690 at 13 (citing to Further Definition of ''Swap,'' ''Security-Based Swap,'' and ''Security-Based Swap Agreement''; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 FR 48208 (Aug. 13, 2012).

definition is broader than the bona fide hedging definition. Under the canons of statutory construction, when Congress writes one section differently than another, the differences should be assumed to have different meaning. Thus, the Commission believes that the more restrictive language in the bona fide hedging definition should be applied here. The definition of bona fide hedging position, as proposed in the December 2013 Position Limits Proposal, as amended by the 2016 Supplemental Position Limits Proposal, and as reproposed here, would be consistent with the differences in the two definitions, as adopted by Congress. The Commission notes that under this Reproposal, commercial end-users may rely on any applicable bona fide hedge exemption.

In response to the commenter's concern regarding ''customary commercial agreements,'' the Commission reiterates its belief that contracts that are exempted or excluded from the definition of ''swap'' are not considered referenced contracts and so are not subject to position limits.

o. Short Position

*Proposed Rule:* The term ''short position'' is currently defined in § 150.1(c) to mean a short call option, a long put option, or a short underlying futures contract. In the December 2013 Position Limits Proposal, the Commission proposed to amend the definition to state that a short position means a short call option, a long put option or a short underlying futures contract, or a short futures-equivalent swap. This proposed revision reflects the fact that under the Dodd-Frank Act, the Commission is charged with applying the position limits regime to swaps.

*Comments Received:* The Commission received no comments regarding the proposed amendment to the definition of ''short position.''

*Commission Reproposal:* Though no commenters suggested changes to the definition of ''short position,'' the Commission is concerned that the proposed definition, like the proposed definition of ''long position'' described supra, does not clearly articulate that futures and options contracts are subject to position limits on a futures-equivalent basis in terms of the core referenced futures contract. Longstanding market practice has applied position limits to futures and options on a futures-equivalent basis, and the Commission believes that practice ought to be made explicit in the definition in order to prevent confusion. Thus, in this Reproposal, the Commission is proposing to amend the definition to clarify that a short position is on a futures-equivalent basis, a short call option, a long put option, a short underlying futures contract, or a swap position that is equivalent to a short futures contract. Though the substance of the definition is fundamentally unchanged, the revised language should prevent unnecessary confusion over the application of futures-equivalency to different kinds of commodity derivative contracts.

p. Speculative Position Limit

The term ''speculative position limit'' is currently not defined in § 150.1. In the December 2013 Position Limits Proposal, the Commission proposed to define the term ''speculative position limit'' to mean ''the maximum position, either net long or net short, in a commodity derivatives contract that may be held or controlled by one person, absent an exemption, such as an exemption for a bona fide hedging position. This limit may apply to a person's combined position in all commodity derivative contracts in a particular commodity (all-months-combined), a person's position in a single month of commodity derivative contracts in a particular commodity, or a person's position in the spot-month of commodity derivative contacts in a particular commodity. Such a limit may be established under federal regulations or rules of a designated contract market or swap execution facility. An exchange may also apply other limits, such as a limit on gross long or gross short positions, or a limit on holding or controlling delivery instruments.'' [356]

As explained in the December 2013 Position Limits Proposal, the proposed definition is similar to definitions for position limits used by the Commission for many years,[357] as well as glossaries published by the Commission for many years.[358] For example, the December 2013 Position Limits Proposal noted that the version of the staff glossary currently posted on the CFTC Web site defines speculative position limit as ''[t]he maximum position, either net long or net short, in one commodity future (or option) or in all futures (or options) of one commodity combined that may be held or controlled by one person (other than a person eligible for a hedge exemption) as prescribed by an exchange and/or by the CFTC.''

The Commission received no comments on the proposed definition, and is reproposing the definition without amendment.

q. Spot-Month

*Proposed Rule:* In the December 2013 Position Limits Proposal, the Commission proposed to adopt a definition of ''spot-month'' that expands upon the current § 150.1 definition.[359] The definition, as proposed, specifically addressed both physical-delivery contracts and cash-settled contracts, and clarified the duration of ''spot-month.'' Under the proposed definition, the ''spot-month'' for physical-delivery commodity derivatives contracts would be the period of time beginning at of the close of trading on the trading day preceding the first day on which delivery notices could be issued or the close of trading on the trading day preceding the third-to-last trading day, until the contract was no longer listed for trading (or available for transfer, such as through exchange for physical transactions). The proposed definition included similar, but slightly different language for cash-settled contracts, providing that the spot month would begin at the earlier of the start of the period in which the underlying cash-settlement price was calculated or the close of trading on the trading day preceding the third-to-last trading day and would continue until the contract

[356] December 2013 Position Limits Proposal, 78 FR at 75825.

[357] *Id.* at 75701. As noted in the December 2013 Position Limits Proposal, ''the various regulations and defined terms included use of maximum amounts 'net long or net short,' which limited what any one person could 'hold or control,' 'one grain on any one contract market' (or in 'in one commodity' or 'a particular commodity'), and 'in any one future or in all futures combined.' For example, in 1936, Congress enacted the CEA, which authorized the CFTC's predecessor, the CEC, to establish limits on speculative trading. Congress empowered the CEC to 'fix such limits on the amount of trading . . . as the [CEC] finds is necessary to diminish, eliminate, or prevent such burden.' [CEA section 6a(1) (Supp. II 1936)] It also noted that the first speculative position limits were issued by the CEC in December 1938, 3 FR 3145, Dec. 24, 1938, and that those first speculative position limits rules provided, also in § 150.1, for limits on position and daily trading in grain for future delivery, and adopted a maximum amount ''net long or net short position which any one person may hold or control in any one grain on any one contract market'' as 2,000,000 bushels ''in any one future or in all futures combined.'' *Id.*

[358] For example, the December 2013 Position Limits Proposal noted that the Commission's annual report for 1983 includes in its glossary ''Position Limit: the maximum position, either net long or net short, in one commodity future combined which may be held or controlled by one person as prescribed by any exchange or by the CFTC.'' *Id.*

[359] December 2013 Position Limits Proposal, 78 FR at 75701–02; As noted in in the December 2013 Position Limits Proposal, the definition proposed would be an expansion upon the definition currently found in § 150.1, but greatly simplified from the definition adopted in vacated § 151.3 (in the Part 151 regulations, the ''spot month'' definition in § 151.1 simply cited to the ''spot month'' definition provided in § 151.3).

cash-settlement price was determined. In addition, the proposed definition included a proviso that, if the cash-settlement price was determined based on prices of a core referenced futures contract during the spot month period for that core referenced futures contract, then the spot month for that cash-settled contract would be the same as the spot month for that core referenced futures contract.[360]

*Comments Received:* The Commission received several comments regarding the definition of spot month.[361] One commenter noted that the definition of the spot month for federal limits does not always coincide with the definition of spot month for purposes of any exchange limits and assumes that the Commission did not intend for this to happen. For example, the commenter noted the proposed definition of spot month would commence at the close of trading on the trading day preceding the first notice day, while the ICE Futures US definition commences as of the opening of trading on the second business day following the expiration of regular option trading on the expiring futures contract. Regarding the COMEX contracts, the commenter stated that the exchange spot month commences at the close of business, rather than at the close of trading, which would allow market participants to incorporate exchange of futures for related position transactions (EFRPs) that occur after the close of trading, but before the close of business.[362] Finally, the commenter requested the Commission ensure the definition of spot month for federal limits is the same as the definition of spot month for exchange limits for all referenced contracts.[363]

Two commenters urged the Commission to reconsider its proposed definition of spot month for cash-settled contracts that encompasses the entire period for calculation of the settlement price, preferring the current exchange practice which is to apply the spot month limit during the last three days before final settlement.[364] One commenter noted its concern that the proposed definition would discourage use of calendar month average price contracts.[365]

Another commenter recommended that the Commission define ''spot month'' in relation to each core referenced futures contract and all related physically-settled and cash-settled referenced contracts, to assure that the definition works appropriately in terms of how each underlying nonfinancial commodity market operates, and to ensure that commercial end-users of such nonfinancial commodities can effectively use such referenced contracts to hedge or mitigate commercial risks.[366]

The Commission also received the recommendation from one commenter that the Commission should publish a calendar listing the spot month for each Core Referenced Futures Contract to provide clarity to market participants and reduce the cost of identifying and tracking the spot month.[367]

*Commission Reproposal:* For core referenced futures contracts, the Commission agrees with the commenter that the definition of spot month for federal limits should be the same as the definition of spot month for exchange limits. The Commission is therefore the definition of spot month in this Reproposal generally follows exchange practices. In the reproposed version, spot month means the period of time beginning at the earlier of the close of business on the trading day preceding the first day on which delivery notices can be issued by the clearing organization of a contract market, or the close of business on the trading day preceding the third-to-last trading day, until the contract expires for physical delivery core referenced futures contracts,[368] except for the following: (a) ICE Futures U.S. Sugar No. 11 (SB) referenced contract for which the spot month means the period of time beginning at the opening of trading on the second business day following the expiration of the regular option contract traded on the expiring futures contract; (b) ICE Futures U.S. Sugar No. 16 (SF) referenced contract,[369] for which the spot month means the period of time beginning on the third-to-last trading day of the contract month until the contract expires [370] and (c) Chicago Mercantile Exchange Live Cattle (LC) referenced contract, for which the spot month means the period of time beginning at the close trading on the fifth business day of the contract month.[371]

As noted above, in the December 2013 Position Limits Proposal, spot month was proposed to be defined to begin at the earlier of: (1) ''the close of trading on the trading day preceding the first day on which delivery notices can be issued to the clearing organization''; or (2) ''the close of trading on the trading day preceding the third-to-last trading day''—based on the comment letters received, the proposed definition resulted in some confusion.[372] The Commission observes that the current definition also seems to be a source of some confusion when it defines ''spot month,'' in current CFTC Regulation 150.1(a), to begin ''at the close of trading on the trading day preceding the first day on which delivery notices can be issued to the clearing organization.''

The Commission understands current DCM practice for physical-delivery contracts permitting delivery before the close of trading generally is that the spot month begins at the start of the first business day on which the clearing house can issue ''stop'' notices to a clearing member carrying a long position, or, at the close of business on the day preceding the first business day on which the clearing house can issue ''stop'' notices to a clearing member carrying a long position, but current DCM rules vary somewhat. For some ICE contracts,[373] the spot month includes ''any month for which delivery notices have been or may be issued,'' [374] and begins at the open of trading; [375] the

[360] *See id.* at 75825–6.

[361] *See, e.g.,* CL–FIA–59595 at 10, CL–NFP–59690 at 19, CL–NGSA–59673 at 44, and CL–ICE–59669 at 5–6.

[362] CL–FIA–59595 at 10.

[363] *Id.*

[364] *See, e.g.,* CL–NGSA–59673 at 44, CL–ICE–59669 at 5–6.

[365] *See,* CL–ICE–59669 at 5–6.

[366] CL–NFP–59690 at 19.

[367] CL–FIA–59595 at 10–11.

[368] As noted above, this Reproposal does not address the three cash-settled contracts (Class III Milk, Feeder Cattle, and Lean Hogs) which, under the December 2013 Position Limits Proposal, were included in the list of core referenced futures contracts. Therefore, the reproposed spot month definition does not address those three contracts.

[369] While the Commission realized that Sugar 16 does not currently have a spot month, its delivery period takes place after the last trading day (similar to crude oil). Therefore, the Reproposal amends the spot month definition for Sugar No. 16 to mirror the three day period for other contracts that deliver after the end of trading.

[370] In regard to the modifier ''until the contract expires,'' the Commission views ''expires'' as meaning the end of delivery period or until cash-settled.

[371] In response to FIA's comment, CL–FIA–59595 at 10, the Commission notes that the spot periods for exchange-set limits on COMEX products begin at the close of trading and not the close of business. *See http://www.cmegroup.com/market-regulation/position-limits.html.* However, the Commission understands that CME Group staff determines compliance with spot month limits in conjunction with the receipt of futures large trader reports. In consideration of the practicality of this approach, and in light of the definition of reportable position, the Commission believes that it would be more practical, clear, and consistent with existing exchange practices, for the spot month to begin ''at the close of the market.'' *See* CFTC Regulation 15.00(p).

[372] As a note of clarification, in light of the confusion of some commenters, position limits apply to open positions; once the position isn't open the limits don't apply.

[373] *See, e.g.,* Cotton No. 2.

[374] *See* ICE Rule 6.19.

[375] *See, e.g.,* Cotton No. 2 Position Limits and Position Accountability information: ''ICE (1) Delivery Month: Cocoa, Coffee ''C'', Cotton, World Cotton, FCOJ, Precious Metals—on and after First Notice Day Sugar#11 on and after the Second

CME spot month, as noted above, begins at the close of trading. However, the Commission understands that the amended ''spot month'' definition, as reproposed herein, would be consistent with the existing spot month practices of exchanges when enforcing the start of the spot month limits in any of the 25 core referenced futures contracts, based on the timing of futures large trader reports, discussed below.

Furthermore, based on Commission staff discussions with staff from several DCMs regarding exchange current practices, the Commission believes that the spot month should begin at the same time as futures large trader reports are submitted—that is, under the definition of reportable position, the spot month should begin ''at the close of the market.'' [376] The Commission views the ''close of the market'' as consistent with ''the close of business.''

In consideration of the practicality of this approach, and in light of the definition of ''reportable position,'' the Commission believes that it would be more practical, clear, and consistent with existing exchange practices, for the spot month to begin ''at the close of business.'' In addition, as noted by one commenter,[377] when the exchange spot month commences at the close of business, rather than at the close of trading, it would allow market participants to incorporate exchange of futures for related position transactions (''EFRPs'') [378] that occur after the close of trading, but before the close of business.

The Commission points out an additional correction made to the reproposed definition, changing it from ''preceding the first day on which delivery notices can be issued *to* the clearing organization of a contract market'' to ''preceding the first day on which delivery notices can be issued by the clearing organization of a contract market'' [emphasis added]. The Commission understands that the spot periods on the exchanges commence the day preceding the first day on which delivery notices can be issued by the clearing organization of a contract market, not the first day on which notices can be issued to the clearing organization. The ''spot month'' definition in this Reproposal, therefore, has been changed to correct this error.

The revisions included in the reproposed definition addresses the concerns of the commenter who suggested the Commission define the spot month according to each core referenced futures contract and for cash-settled and physical delivery referenced contracts that are not core referenced futures contracts, although for clarity and brevity the Commission has chosen to highlight contracts that are the exception to the general definition rather than list each of the 25 core referenced futures contracts and multitude of referenced contracts separately.

In response to the commenters' concern regarding cash-settled referenced contracts, the Reproposal changes the definition of spot month to agree with the limits proposed in § 150.2. In the December 2013 Position Limits Proposal, the Commission defined the spot month for certain cash-settled referenced contracts, including calendar month averaging contracts, to be a longer period than the spot month period for the related core referenced futures contract. However, the Commission did not propose a limit for such contracts in proposed § 150.2, rendering superfluous that aspect of the proposed definition of spot month, at this time. The Commission is reproposing the definition of spot month without this provision, thereby addressing the concerns of the commenters regarding the impact of the definition on calendar month averaging contracts outside of the spot month for the relevant core referenced futures contract. In order to make clearer the relevant spot month periods for referenced contracts other than core referenced futures contracts, the Commission has included subsection (3) of the definition that states that the spot month for such referenced contracts is the same period as that of the relevant core referenced futures contract.

The Commission believes that the revised definition reproposed here sufficiently clarifies the applicable spot month periods, which can also be determined via exchange rulebooks and defined contract specifications, such that a defined calendar of spot months is not necessary. Further, a published calendar would need to be revised every year to update spot month periods for each contract and each expiration. The Commission believes this constant revision may lead to more confusion than it is meant to correct.

r. Spot-Month, Single-Month, and All-Months-Combined Position Limits

*Proposed Rule:* In addition to a definition for ''spot month,'' current part 150 includes definitions for ''single month,'' and for ''all-months'' where ''single month'' is defined as ''each separate futures trading month, other than the spot month future,'' and ''all-months'' is defined as ''the sum of all futures trading months including the spot month future.''

As noted in the December 2013 Position Limits proposal, vacated part 151 retained only the definition for spot month, and, instead, adopted a definition for ''spot-month, single-month, and all-months-combined position limits.'' The definition specified that, for Referenced Contracts based on a commodity identified in § 151.2, the maximum number of contracts a trader could hold was as provided in § 151.4.

In the December 2013 Position Limits Proposal, as noted above, the Commission proposed to amend § 150.1 by deleting the definitions for ''single month,'' and for ''all-months,'' but, unlike the vacated part 151, the proposal did not include a definition for ''spot-month, single-month, and all-months-combined position limits.'' Instead, it proposed to adopt a definition for ''speculative position limits'' that should obviate the need for these definitions.[379]

*Comments Received:* The Commission received no comments regarding the deletion of these definitions.

*Commission Reproposal:* This Reproposal, consistent with the December 2013 Position Limits Proposal, eliminates the definitions for ''single month,'' and for ''all-months,'' for the reasons provided above.

s. Swap and Swap Dealer

*Proposed Rule:* While the terms ''swap'' and ''swap dealer'' are not currently defined in § 150.1, the December 2013 Position Limits Proposal amended § 150.1 to define these terms as they are defined in section 1a of the Act and as further defined in section 1.3 of this chapter.'' [380]

*Comments Received:* The Commission received no comments on these definitions.

Business Day following the expiration of the regular option contract traded on the expiring futures contract.'' *https://www.theice.com/products/254/Cotton-No-2-Futures*.

[376] *See* current § 15.00(p).

[377] CL–FIA–59595 at 10.

[378] The Commission notes that DCM determinations of allowable blocks, EFRPs, and transfer trades, in regards to position limits, must also consider compliance with DCM Core Principle 9; discussion of the interplay is beyond the scope of this Reproposal.

[379] *See* Section III.A.1.r (Spot-month, single-month, and all-months-combined position limits) above for a discussion of the proposed definition of ''speculative position limit.''

[380] 7 U.S.C. 1a(47) and 1a(49); § 1.3(xxx) (''swap'') and § 1.3(ggg) (''swap dealer''). *See* Further Definition of ''Swap Dealer,'' ''Security-Based Swap Dealer,'' ''Major Swap Participant,'' ''Major Security-Based Swap Participant'' and ''Eligible Contract Participant,'' 77 FR 30596 (May 23, 2012); *see also,* Swap Definition Rulemaking.

*Commission Reproposal:* The Commission has determined to repropose these definitions as originally proposed, for the reasons provided above.

2. Bona Fide Hedging Definition

a. Bona Fide Hedging Position (BFH) Definition—Background

Prior to the 1974 amendments to the CEA, the definition of a bona fide hedging position was found in the statute. The 1974 amendments authorized the newly formed Commission to define a bona fide hedging position.[381] The Commission published a final rule in 1977, providing a general definition of a bona fide hedging position in § 1.3(z)(1).[382] The Commission listed certain positions, meeting the requirements of the general definition of a bona fide hedging position, in § 1.3(z)(2) (*i.e.,* enumerated bona fide hedging positions). The Commission provided an application process for market participants to seek recognition of non-enumerated bona fide hedging positions in §§ 1.3(z)(3) and 1.48.

During the 1980's, exchanges were required to incorporate the Commission's general definition of bona fide hedging position into their exchange-set position limit regulations.[383] While the Commission had established position limits on only a few commodity futures contracts in § 150.2, Commission rule § 1.61 (subsequently incorporated into § 150.5) required DCMs to establish limits on commodities futures not subject to federal limits. The Commission directed in § 1.61(a)(3) (subsequently incorporated into § 150.5(d)(1)) that no DCM regulation regarding position limits would apply to bona fide hedging positions as defined by a DCM in accordance with § 1.3(z)(1).

In 1987, the Commission provided interpretive guidance regarding the bona fide hedging definition and risk management exemptions for futures in financial instruments (now termed excluded commodities).[384] This guidance permitted exchanges, for purposes of exchange-set limits on excluded commodities, to recognize risk management exemptions.[385]

In the 1990's, the Commission allowed exchanges to experiment with substituting position accountability levels for position limits.[386] The CFMA, in 2000, codified, in DCM Core Principle 5, position accountability as an acceptable practice.[387] The CFMA, however, did not address the definition of a bona fide hedging position.

With the passing of the CFMA in 2000, the Commission's requirements for exchanges to adopt position limits and associated bona fide hedging exemptions, in § 150.5, were rendered mere guidance. That is, exchanges were no longer required to establish limits and no longer required to use the Commission's general definition of a bona fide hedging position. Nonetheless, the Commission continued to guide exchanges to adopt position limits, particularly for the spot month in physical-delivery physical commodity derivatives, and to provide for exemptions.

The Farm Bill of 2008 authorized the Commission to regulate swaps traded on exempt commercial markets (ECM) that the Commission determined to be a significant price discovery contract (SPDC).[388] The Commission implemented these provisions in part 36 of its rules.[389] The Commission provided guidance to ECMs in complying with Core Principle IV regarding position limitations or accountability.[390] That guidance provided, as an acceptable practice for cleared trades, that the ECM's position limit rules may exempt bona fide hedging positions.

In 2010, the Dodd-Frank Act added a directive, for purposes of implementation of CEA section 4a(a)(2), for the Commission to define a bona fide hedging position for physical commodity derivatives consistent with, in the Commission's opinion, the reasonably certain statutory standards in CEA section 4a(c)(2). Those statutory standards build on, but differ slightly from, the Commission's general definition in rule 1.3(z)(1).[391] The Commission interprets those statutory standards as directing the Commission to narrow the bona fide hedging position definition for physical commodities.[392] The Commission discusses those differences, below.

b. BFH Definition Summary

Under the December 2013 Position Limits Proposal, the Commission proposed a new definition of bona fide hedging position, to replace the current definition in § 1.3(z), that would be applicable to positions in excluded commodities and in physical commodities.[393] The proposed definition was organized into an opening paragraph and five numbered paragraphs. In the opening paragraph, for positions in either excluded commodities or physical commodities, the proposed definition would have applied two general requirements: The incidental test; and the orderly trading requirement. For excluded commodities, the Commission proposed in paragraph (1) a definition that conformed to the Commission's 1987

[381] Those amendments to CEA section 4a(3), subsequently re-designated § 4a(c)(1), 7 U.S.C. 6a(c)(1), provide that no rule of the Commission shall apply to positions which are shown to be bona fide hedging positions, as such term is defined by the Commission. *See,* sec. 404 of the Commodity Futures Trading Commission Act of 1974, Pub. L. 93–463, 88 Stat. 1389 (Oct. 23, 1974). *See* 2013 Position Limits Proposal, 78 FR at 75703 for additional discussion of the history of the definition of a bona fide hedging position.

[382] 42 FR 42748 (Aug. 24, 1977). Previously, the Secretary of Agriculture, pursuant to section 404 of the Commodity Futures Trading Commission Act of 1974 (Pub. L. 93–463), promulgated a definition of bona fide hedging transactions and positions. 40 FR 111560 (March 12, 1975). That definition, largely reflecting the statutory definition previously in effect, remained in effect until the newly-established Commission defined that term. *Id.*

[383] 46 FR 50938 at 50945 (Oct. 16, 1981).

[384] 52 FR 34633 (Sept. 14, 1987) and 52 FR 27195 (July 20, 1987).

[385] *See* December 2013 Position Limits Proposal, 78 FR at 75704.

[386] Exchange rules for position accountability levels require a market participant whose position exceeds an accountability level to consent automatically to requests of the exchange: (1) To provide information about a position; and (2) to not increase or to reduce a position, if so ordered by the exchange. In contrast, a speculative position limit rule does not authorize an exchange to order a market participant to reduce a position. Rather, a position limit sets a maximum permissible size for a speculative position. The Commission notes that it may require a market participant to provide information about a position, for example, by issuing a special call under § 18.05 to a trader with a reportable position in futures contracts.

[387] DCM Core Principle 5 is codified in CEA section 5(d)(5), 7 U.S.C. 7(d)(5). *See* Section 111 of the Commodity Futures Modernization Act of 2000, Pub. L. No. 106–554, 114 Stat. 2763 (Dec. 21, 2000) (CFMA).

[388] *See* § 13201 of the Food, Conservation and Energy Act of 2008, Pub. L. No. 110–246, 122 Stat. 1624 (June 18, 2008) (Farm Bill of 2008). These provisions were subsequently superseded by the Dodd-Frank Act.

[389] 66 FR 42270 (Aug. 10, 2001). Part 36 was removed and reserved to conform to the amendments to the CEA by the Dodd-Frank Act.

[390] 17 CFR part 36, App. B (2010).

[391] It should be noted that a 2011 final rule of the Commission would have amended the definition of a bona fide hedging position in § 1.3(z), to be applicable only to excluded commodities, and would have added a new definition of a bona fide hedging position to Part 151, to be applicable to physical commodities. Position Limits for Futures and Swaps, 76 FR 71626 (Nov.18, 2011). However, prior to the compliance date for that 2011 rulemaking, a federal court vacated most provisions of that rulemaking, including the amendments to the definition of a bona fide hedging position. *International Swaps and Derivatives Ass'n* v. *United State Commodity Futures Trading Comm'n,* 887 F. Supp. 2d 259 (D.D.C. 2012). Because the Commission has not instructed **Federal Register** to roll back the 2011 changes to the CFR, the current definition of a bona fide hedging position is found in the 2010 version of the Code of Federal Regulations. 17 CFR 1.3(z) (2010).

[392] *See* December 2013 Position Limits Proposal, 78 FR at 75705.

[393] *See* December 2013 Position Limits Proposal, 78 FR at 75702–23. In doing so, the Commission proposed to remove and reserve § 1.3(z).

interpretations permitting risk management exemptions in excluded commodity contracts. For physical commodities, the Commission proposed in paragraph (2) to amend the current general definition to conform to CEA section 4a(c) and to remove the application process in §§ 1.3(z)(3) and 1.48, that permits market participants to seek recognition of non-enumerated bona fide hedging positions. Rather, the Commission proposed that a market participant may request either a staff interpretative letter under § 140.99 [394] or seek CEA section 4a(a)(7) exemptive relief.[395] Paragraphs (3) and (4) listed enumerated exemptions. Paragraph (5) listed the requirements for cross-commodity hedges of enumerated exemptions.

In response to comments on the December 2013 Position Limits Proposal, in the 2016 Supplemental Proposal, the Commission amended the proposed definition of bona fide hedging position.[396] The amended definition proposed in the 2016 Supplemental Proposal would no longer apply the two general requirements (the incidental test and the orderly trading requirement). For excluded commodities, the Commission again proposed paragraph (1) of the definition, substantially as in 2013. For physical commodities, the Commission again proposed to conform paragraph (2) more closely to CEA section 4a(c), but also proposed an application process for market participants to seek recognition of non-enumerated bona fide hedging positions, without the need to petition the Commission. The Commission again proposed paragraphs (3) through (5).

In response to comments on both the December 2013 Position Limits Proposal and the 2016 Supplemental Proposal, the Commission is now reproposing the definition of bona fide hedging position, generally as proposed in the 2016 Supplemental Proposal, but with a few further amendments. First, for excluded commodities, the Commission clarifies further the discretion of exchanges in recognizing risk management exemptions. Second, for physical commodities, the Commission: (a) Clarifies the scope of the general definition of a bona fide hedging position; (b) conforms that general definition more closely to CEA section 4a(c) by including recognition of positions that reduce risks attendant to a swap that was used as a hedge; and, (c) re-organizes additional requirements for enumerated hedges and requirements for other recognition as a non-enumerated bona fide hedging position, apart from the general definition.

c. BFH Definition Discussion—Remove Incidental Test and Orderly Trading Requirement

*Proposed Rule:* As noted above, the Commission proposed to retain, in its December 2013 Position Limits Proposal,[397] then proposed to remove, in its 2016 Supplemental Position Limits Proposal,[398] two general requirements contained in the § 1.3(z)(1) definition of bona fide hedging position: the incidental test; and the orderly trading requirement. The incidental test requires, for a position to be recognized as a bona fide hedging position, that the ''purpose is to offset price risks incidental to commercial cash, spot, or forward operations.'' The orderly trading requirement mandates that ''such position is established and liquidated in an orderly manner in accordance with sound commercial practices.''

*Comments Received:* Commenters generally objected to retaining the incidental test and the orderly trading requirement in the definition of bona fide hedging position, as proposed in 2013.[399] A number of commenters supported the Commission's 2016 Supplemental Proposal to remove the incidental test and the orderly trading requirement.[400]

Incidental Test: Commenters objected to the incidental test, because that test is not included in the standards in CEA section 4a(c) for the Commission to define a bona fide hedging position for physical commodities.[401]

However, other commenters noted their belief that eliminating the incidental test would permit swap dealers or purely financial entities to avail themselves of bona fide hedging exemptions, to the detriment of commercial hedgers.[402]

Orderly trading requirement: One commenter urged the Commission to eliminate the orderly trading requirement, because this requirement does not apply to over-the-counter markets, the Commission does not define orderly trading in a bi-lateral market, and this requirement imposes a duty on end users to monitor market activities to ensure they do not cause a significant market impact; additionally, the commenter noted the anti-disruptive trading prohibitions and polices apply regardless of whether the orderly trading requirement is imposed.[403] Similarly, another commenter urged the Commission to exempt commercial end-users from the orderly trading requirement, arguing that an orderly trading requirement unreasonably requires commercial end-users to monitor markets to measure the impact of their activities without clear guidance from the Commission on what would constitute significant market impact.[404]

Other commenters to the 2013 Proposal requested the Commission interpret the orderly trading requirement consistently with the Commission's disruptive trading practices interpretation (*i.e.,* a standard of intentional or reckless conduct) and not to apply a negligence standard.[405] Yet another commenter requested clarification on the process the Commission would use to determine whether a position has been established and liquidated in an orderly manner, whether any defenses may be available, and what would be the consequences of failing the requirement.[406]

However, one commenter is concerned that eliminating the orderly trading requirement for bona fide hedging for swaps positions would discriminate against market participants in the futures and options markets. The commenter noted that, if the Commission eliminates this requirement, the Commission could not use its authority effectively to review exchange-granted exemptions for swaps from position limits to prevent or diminish excessive speculation.[407]

*Commission Reproposal:* In the reproposed definition of bona fide hedging position, the Commission is eliminating the incidental test and the orderly trading requirement.

Incidental Test: Under the Reproposal, the incidental test has been eliminated, because the Commission views the economically appropriate test (discussed below) as including the concept of the offset of price risks

[394] Section 140.99 sets out general procedures and requirements for requests to Commission staff for exemptive, no-action and interpretative letters.

[395] *See* December 2013 Position Limits Proposal, 78 FR 75719.

[396] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38462–64.

[397] 78 FR at 75706.

[398] 81 FR at 38462.

[399] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38462.

[400] *See, e.g.,* CL–NCFC–60930 at 2, CL–FIA–60937 at 5 and 23, and CL–IECAssn–60949 at 5–7.

[401] *See, e.g.,* CL–CME–58718 at 47, and CL–NGFA–60941 at 2.

[402] *See, e.g.,* CL–IATP–60951 at 4, CL–AFR–60953 at 2, CL–Better Markets–60928 at 5, and CL–Rutkowski–60962 at 1.

[403] *See* CL–COPE–59662 at 13.

[404] *See* CL–DEU–59627 at 5–7.

[405] *See, e.g.,* CL–FIA–59595 at 5, 33–34, CL–EEI–EPSA–59602 at 14–15, CL–ISDA/SIFMA–59611 at 4, 39, CL–CME–59718 at 67, and CL–ICE–59669 at 11.

[406] *See* CL–Working Group–59693 at 14.

[407] *See* CL–IATP–60951 at 4.

incidental to commercial cash, spot, or forward operations. It was noted in the 2013 Position Limits Proposal that, ''The Commission believes the concept of commercial cash market activities is also embodied in the economically appropriate test for physical commodities in [CEA section 4a(c)(2)].'' [408] It should be noted the incidental test has been part of the regulatory definition of bona fide hedging since 1975,[409] but that the requirement was not explained in the 1974 proposing notice (''proposed definition otherwise deviates in only minor ways from the hedging definition presently contained in [CEA section 4a(3)]'').[410]

The Commission is not persuaded by the commenters who believe eliminating the incidental test would permit financial entities to avail themselves of a bona fide hedging exemption, because the incidental test is essentially embedded in the economically appropriate test. In addition, for a physical-commodity derivative, the reproposed definition, in mirroring the statutory standards of CEA section 4a(c), requires a bona fide hedging position to be a substitute for a transaction taken or to be taken in the cash market (either for the market participant itself or for the market participant's pass-through swap counterparty), which generally would preclude financial entities from availing themselves of a bona fide hedging exemption (in the absence of qualifying for a pass-through swap offset exemption, discussed below).

Orderly Trading Requirement: The Reproposal also eliminates the orderly trading requirement. That provision has been a part of the regulatory definition of bona fide hedging since March 12, 1975 [411] and previously was found in the statutory definition of bona fide hedging position prior to the 1974 amendment removing the statutory definition from CEA section 4a(3). However, the Commission is not aware of a denial of recognition of a position as a bona fide hedging position, as a result of a lack of orderly trading. Further, the Commission notes that the meaning of the orderly trading requirement is unclear in the context of the over-the-counter (OTC) swap market or in the context of permitted off-exchange transactions (*e.g.,* exchange of futures for physicals).

In regard to the anti-disruptive trading prohibitions of CEA section 4c(a)(5), those prohibitions apply to trading on registered entities, but not to OTC transactions. It should be noted that the anti-disruptive trading prohibitions in CEA section 4c(a)(5) make it unlawful to engage in trading on a registered entity that ''demonstrates intentional or reckless disregard for orderly execution of trading during the closing period'' (emphasis added); however, the Commission has not, under the authority of CEA section 4c(a)(6), prohibited the intentional or reckless disregard for the orderly execution of transactions on a registered entity outside of the closing period.

The Commission notes that an exchange may impose a general orderly trading on all market participants. Market participants may request clarification from exchanges on their trading rules. The Commission does not believe that the absence of an orderly trading requirement in the definition of bona fide hedging position would discriminate against any particular trading venue for commodity derivative contracts.

d. BFH Definition Discussion—Excluded Commodities

*Proposed Rule:* In both the 2013 Position Limits Proposal and the 2016 Supplement Proposal, the proposed definition of bona fide hedging position for contracts in an excluded commodity included a standard that the position is economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise (the economically appropriate test) and also specified that such position should be either (i) specifically enumerated in paragraphs (3) through (5) of the definition of bona fide hedging position; or (ii) recognized as a bona fide hedging position by a DCM or SEF consistent with the guidance on risk management exemptions in proposed Appendix A to part 150.[412] As noted above, the 2016 Supplemental Proposal would eliminate the two additional general requirements (the incidental test and the orderly trading requirement).

*Comments Received:* One commenter believed that, to avoid an overly restrictive definition due to the limited set of examples provided by the Commission, only the general definition of a bona fide hedging position should be applicable to hedges of an excluded commodity.[413]

*Commission Reproposal:* After consideration of comments and review of the record, the Commission has determined in the Reproposal to apply the economically appropriate test to enumerated exemptions, as proposed.[414] However, the Reproposal amends the proposed definition of a bona fide hedging position for an excluded commodity, to clarify that an exchange may otherwise recognize risk management exemptions in an excluded commodity, without regard to the economically appropriate test. Regarding risk management exemptions, the Commission notes that Appendix A (which codifies the Commission's two 1987 interpretations of the bona fide hedging definition in the context of excluded commodities) includes examples of risk altering transactions, such as a temporary increase in equity exposure relative to cash bond holdings. Such risk altering transactions appear inconsistent with the Commission's interpretation of the economically appropriate test. Accordingly, the Reproposal removes the economically appropriate test from the guidance for exchange-recognized risk management exemptions in excluded commodities.

Regarding an exchange's obligation to comply with core principles pertaining to position limits on excluded commodities, as discussed further in § 150.5, the Commission clarifies that under the Reproposal, exchanges have reasonable discretion as to whether to adopt the Commission's definition of a bona fide hedging position, including whether to grant risk management exemptions, such as those that would be consistent with, but not limited to, the examples in Appendix A to part 150. That is, the set of examples in Appendix A to part 150 is non-restrictive, as it is guidance. The Reproposal also makes minor wording changes in Appendix A to part 150, including to clarify an exchange's reasonable discretion in granting risk management exemptions and to eliminate a reference to the orderly trading requirement which has been deleted, as discussed above, but otherwise is adopting Appendix A as proposed.

e. BFH Definition Discussion—Physical Commodities General Definition

As noted in its proposal, the core of the Commission's approach to defining bona fide hedging over the years has focused on transactions that offset a

[408] *See* December 2013 Position Limits Proposal, 78 FR at 75707.

[409] 40 FR 11560 (March 12, 1975).

[410] 39 FR 39731 (Nov. 11, 1974).

[411] 40 FR 11560 (Mar. 12, 1975).

[412] December 2013 Position Limits Proposal, 78 FR at 75707; 2016 Supplemental Position Limits Proposal, 81 FR at 38505.

[413] CL–BG Group–59656 at 9.

[414] The Commission did not propose to apply to excluded commodities any of the additional standards in the general definition applicable to hedges of a physical commodity.

recognized price risk.[415] Once a bona fide hedge is implemented, the hedged entity should be price insensitive because any change in the value of the underlying physical commodity is offset by the change in value of the entity's physical commodity derivative position.

Because a firm that has hedged its price exposure is price neutral in its overall physical commodity position, the hedged entity should have little incentive to manipulate or engage in other abusive market practices to affect prices. By contrast, a party that maintains a derivative position that leaves it with exposure to price changes is not neutral as to price and, therefore, may have an incentive to affect prices. Further, the intention of a hedge exemption is to enable a commercial entity to offset its price risk; it was never intended to facilitate taking on additional price risk.

The Commission recognizes there are complexities to analyzing the various commercial price risks applicable to particular commercial circumstances in order to determine whether a hedge exemption is warranted. These complexities have led the Commission, from time to time, to issue rule changes, interpretations, and exemptions. Congress, too, has periodically revised the Federal statutes applicable to bona fide hedging, most recently in the Dodd-Frank Act.

CEA section 4a(c)(1),[416] as re-designated by the Dodd-Frank Act, authorizes the Commission to define bona fide hedging positions ''consistent with the purposes of this Act.'' CEA section 4a(c)(2), as added by the Dodd-Frank Act, provides new requirements for the Commission to define bona fide hedging positions in physical commodity derivatives ''[f]or the purposes of implementation of [CEA section 4a(a)(2)] for contracts of sale for future delivery or options on the contracts of commodities [traded on DCMs].'' [417]

*General Definition:* The Commission's proposed general definition for physical commodity derivative contracts, mirroring CEA section 4a(c)(2)(a), specifies a bona fide hedging position is one that:

(a) *Temporary substitute test:* represents a substitute for transactions made or to be made or positions taken or to be taken at a later time in the physical marketing channel;

(b) *Economically appropriate test:* is economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise; and

(c) *Change in value requirement:* arises from the potential change in the value of assets, liabilities, or services, whether current or anticipated.

In addition to the above, the Commission's proposed general definition, mirroring CEA section 4a(c)(2)(B)(i), also recognizes a bona fide hedging position that:

(d) *Pass-through swap offset:* reduces risks attendant to a position resulting from a swap that was executed opposite a counterparty for which the transaction would qualify as a bona fide hedging transaction under the general definition above.

The Commission proposed another provision, based on the statutory standards, to recognize as a bona fide position that:

(e) *Pass-through swap:* is itself the swap executed opposite a pass-through swap counterparty, provided that the risk of that swap has been offset.

The Commission received a number of comments on the December 2013 Position Limits Proposal and the 2016 Supplemental Proposal. Those concerning the incidental test and the orderly trading requirement are discussed above. Others are discussed below.

i. Temporary Substitute Test and Risk Management Exemptions

*Proposed Rule:* The temporary substitute test is discussed in the 2013 Position Limits Proposal at 75708–9. As the Commission noted in the proposal, it believes that the temporary substitute test is a necessary condition for classification of positions in physical commodities as bona fide hedging positions. The proposed test mirrors the statutory test in CEA section 4a(c)(2)(a)(i). The statutory test does not include the adverb ''normally'' to modify the verb ''represents'' in the phrase ''represents a substitute for transactions taken or to be taken at a later time in a physical marketing channel.'' Because the definition in § 1.3(z)(1) includes the adverb ''normally,'' the Commission interpreted that provision to be merely a temporary substitute criterion, rather than a test. Accordingly, the Commission previously granted risk management exemptions for persons to offset the risk of swaps and other financial instruments that did not represent substitutes for transactions or positions to be taken in a physical marketing channel. However, given the statutory change in direction, positions that reduce the risk of such speculative swaps and financial instruments would no longer meet the requirements for a bona fide hedging position under the proposed definition in § 150.1.

*Comments Received:* A number of commenters urged the Commission not to deny risk-management exemptions for financial intermediaries who utilize referenced contracts to offset the risks arising from the provision of diversified, commodity-based returns to the intermediaries' clients.[418]

However, other commenters noted the ''proposed rules properly refrain from providing a general exemption to financial firms seeking to hedge their financial risks from the sale of commodity-related instruments such as index swaps, Exchange Traded Funds (ETFs), and Exchange Traded Notes (ETNs),'' because such instruments are inherently speculative and may overwhelm the price discovery function of the derivative market.[419]

*Commission Reproposal:* The Reproposal would retain the temporary substitute test, as proposed. The Commission interprets the statutory temporary substitute test as more stringent than the temporary substitute criterion in § 1.3(z)(1);[420] that is, the Commission views the statutory test as narrowing the standards for a bona fide hedging position. Further, the Commission believes that retaining a risk management exemption for swap intermediaries, without regard to the purpose of the counterparty's swap, would fly in the face of the statutory restrictions on pass-through swap offsets (requiring the position of the pass-through swap counterparty to

[415] December 2013 Position Limits Proposal, 78 FR at 75702–3.

[416] 7 U.S.C. 6a(c)(1).

[417] The Reproposal provides for a phased approach to implementation of CEA section 4a(a)(2), to reduce the potential administrative burden on exchanges and market participants, and to facilitate adoption of monitoring policies, procedures and systems. *See, e.g.,* December 2013 Position Limits Proposal, 78 FR at 75725. The first phase of implementation of CEA section 4a(a)(2), in this Reproposal, initially sets federal limits on 25 core referenced futures contracts and their associated referenced contracts. The Commission is establishing a definition of bona fide hedging position for physical commodities in connection with its implementation of CEA section 4a(a)(2), applicable to federal limits. However, the Reproposal does not mandate adoption of that definition of a bona fide hedging position for purposes of exchange-set limits in contracts that are not yet subject to a federal limit. *See* below regarding guidance and requirements under reproposed § 150.5 for exchange-set limits in physical commodities.

[418] *See, e.g.,* CL–FIA–59595 at 5, 34–35; CL–AMG–59709 at 2, 12–15; and CL–CME–59718 at 67–69.

[419] *See, e.g.,* CL–Sen. Levin–59637 at 8, and CL–Better Markets–60325 at 2.

[420] *See* December 2013 Position Limits Proposal, 78 FR at 75709.

qualify as a bona fide hedging transaction).[421]

*Proposed Rule on risk management exemption grandfather provisions:* The Commission proposed in § 150.2(f) and § 150.3(f) to grandfather previously granted risk-management exemptions, as applied to pre-existing positions.[422]

*Comments Received:* Commenters requested that the Commission extend the grandfather relief to permit pre-existing risk management positions to be increased after the effective date of a limit.[423] Commenters also requested that the Commission permit the risk associated with a pre-existing position to be offset by a futures position in a deferred contract month, after the liquidation of an offsetting position in a nearby futures contract month.[424]

Some commenters urged the Commission not to deny risk-management exemptions for financial intermediaries who utilize referenced contracts to offset the risks arising from the provision of diversified commodity-based returns to the intermediaries' clients.[425]

In contrast, other commenters noted that the proposed rules ''properly refrain'' from providing a general exemption to financial firms seeking to hedge their financial risks from the sale of commodity-related instruments such as index swaps, ETFs, and ETNs because such instruments are ''inherently speculative'' and may overwhelm the price discovery function of the derivative market.[426] Another commenter noted, because commodity index contracts are speculative, the Commission should not provide a regulatory exemption for such contracts.[427]

*Commission Reproposal:* The Reproposal clarifies and expands the relief in § 150.3(f) (previously granted exemptions) by: (1) Clarifying that such previously granted exemptions may apply to pre-existing financial instruments that are within the scope of existing § 1.47 exemptions, rather than only to pre-existing swaps; and (2) recognizing exchange-granted non-enumerated exemptions in non-legacy commodity derivatives outside of the spot month (consistent with the Commission's recognition of risk management exemptions outside of the spot month), and provided such exemptions are granted prior to the compliance date of the final rule, once adopted, and apply only to pre-existing financial instruments as of the effective date of that final rule. These two changes are intended to reduce the potential for market disruption by forced liquidations, since a market intermediary would continue to be able to offset risks of pre-effective-date financial instruments, pursuant to previously-granted federal or exchange risk management exemptions.

The Reproposal clarifies that the Commission will continue to recognize the offset of the risk of a pre-existing financial instrument as bona fide using a derivative position, including a deferred derivative contract month entered after the effective date of a final rule, provided a nearby derivative contract month is liquidated. However, under the Reproposal, such relief will not be extended to an increase in positions after the effective date of a limit, because that appears contrary to Congressional intent to narrow the definition of a bona fide hedging position, as discussed above.

ii. Economically Appropriate Test

*Commission proposal:* The economically appropriate test is discussed in the 2013 Position Limits Proposal at 75709–10. The proposed economically appropriate test mirrors the statutory test, which, in turn, mirrors the test in current § 1.3(z)(1).

*Comments received:* Several commenters requested that the Commission broadly interpret the phrase ''economically appropriate'' to include more than just price risk, stating that there are other types of risk that are economically appropriate to address in the management of a commercial enterprise including operational risk, liquidity risk, credit risk, locational risk, and seasonal risk.[428]

Commenters suggested that if the Commission objected to expanding its interpretation of ''economically appropriate'' risks, then the Commission should allow the exchanges to utilize discretion in their interpretations of the economically appropriate test.[429] Another commenter believed that the Commission should provide ''greater flexibility'' in the various bona fide hedging tests, because hedging that reduces all the various types of risk should be deemed ''economically appropriate.''[430] Commenters suggested that a broader view of the types of risks considered to be ''economically appropriate'' should not be perceived as being at odds with the Commission's view of ''price risk'' because all of these risks can inform and determine price, noting that firms evaluate different risks and determine a price impact based on a combination of their likelihood of occurrence and the price impact in the event of occurrence.[431]

*Commission Reproposal:* The Reproposal does not broaden the interpretation of the phrase ''economically appropriate.'' The Commission notes that it has provided interpretations and guidance over the years as to the meaning of ''economically appropriate.''[432] The Commission reiterates its view that, to satisfy the economically appropriate test and the change in value requirement of CEA section 4a(c)(2)(A)(iii), the purpose of a bona fide hedging position must be to offset price risks incidental to a commercial enterprise's cash operations.[433]

The Commission notes that an exchange is permitted to recognize non-enumerated bona fide hedging positions under the process of § 150.9, discussed below, subject to assessment of the particular facts and circumstances, where price risk arises from other types of risk. The Reproposal does not, however, allow the exchanges to utilize unbounded discretion in interpreting ''economically appropriate'' in such recognitions. The Commission believes that such a broad delegation is not authorized by the CEA and, in the Commission's view, would be contrary to the reasonably certain statutory standard of the economically appropriate test. Further, as explained in the discussion of § 150.9, exchange determinations will be subject to the Commission's *de novo* review.

*Comments on gross vs. net hedging:* A number of commenters requested that the Commission recognize as bona fide both ''gross hedging'' and ''net hedging,'' without regard to overall risk.[434] Commenters generally requested, as ''gross hedging,'' that an enterprise should be permitted the flexibility to use either a long or short derivative to offset the risk of any cash position, identified at the discretion of

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[421] *See* CEA section 4a(c)(2)(B)(i).

[422] *See* December 2013 Position Limits Proposal, 78 FR at 75734–5 and 75739–41.

[423] *See, e.g.,* CL–AMG–59709 at 2, 18.

[424] *See, e.g., id.* at 18–19.

[425] CL–FIA–59595 at 5,34–35; CL–AMG–59709 at 2, 12–15; and CL–CME–59718 at 67–69.

[426] CL–Sen. Levin–59637 at 8; and CL–Better Markets–60325 at 2.

[427] CL–CMOC–59720 at 4–5.

[428] *See, e.g.,* CL–NCGA–NGSA–60919 at 4, CL–EEI–EPSA–60925 at 14, CL–API–60939 at 2, CL–CMC–60950 at 4–5, CL–NCFC–60930 at 2, CL–ADM–60934 at 2–6, CL–FIA–60937 at 5 and 20, CL–NGFA–60941 at 4, and CL–Associations–60972 at 2.

[429] *See, e.g.,* CL–CMC–60950 at 4–5, and CL–Olam–59946 at 2–4.

[430] CL–ICE–60929 at 10.

[431] *See, e.g.,* CL–ADM–60934 at 2–6, and CL–API–60939 at 2.

[432] *See* December 2013 Position Limits Proposal, 78 FR at 75709–10.

[433] *Id.* at 75710.

[434] *See, e.g.,* CL–MGEX–60936 at 11, CL–CMC–60950 at 6, CL–Associations–60972 at 2.

the commercial enterprise, irrespective of the commercial enterprise's net cash market position.[435] For example, a commenter contended that a commercial enterprise should be able to hedge fixed-price purchase contracts (*e.g.,* with a short futures position), without regard to the enterprise's fixed-price sales contracts, even if such a short derivative position may increase the enterprise's risk.[436] One commenter stated that the ''new proposed interpretation'' of the ''economically appropriate'' test requires a commercial enterprise to include, and consider for purposes of bona fide hedging, portions of its portfolio it would not otherwise consider in managing risk.[437] Another commenter did not agree that market participants should be required to calculate risk on a consolidated basis, because this approach would require commercial entities to build out new systems. As an alternative, that commenter requests the Commission recognize current risk management tools.[438]

*Commission Reproposal:* The Reproposal retains the Commission's interpretation, as proposed, of economically appropriate gross hedging: that in circumstances where net hedging does not measure all risk exposures, an enterprise may appropriately enter into, for example, a calendar month spread position as a gross hedge. A number of comments misconstrued the Commission's historical interpretation of gross and net hedging. The Commission has not recognized selective identification of cash positions to justify a position as bona fide; rather, the Commission has permitted a regular practice of excluding certain commodities, products, or by-products, in determining an enterprise's risk position.[439] As proposed, the Reproposal requires such excluded commodities to be *de minimis* or difficult to measure, because a market participant should not be permitted to ignore material cash market positions and enter into derivative positions that increase risk while avoiding a position limit restriction; rather, such a market participant's speculative activity must remain below the level of the speculative position limit.

Note, however, under a partial reading of a preamble to a 1977 proposal, the Commission has appeared to recognize gross hedging, without regard to net risk, as bona fide; the Commission noted in 1977 that: ''The previous statutory definition of bona fide hedging transactions or positions contained in section 4a of the Act before amendment by the CFTC Act and the present definition permit persons to classify as hedging any purchase or sale for future delivery which is offset by their gross cash position irrespective of their net cash position.'' [440] However, under a full reading of that 1977 proposal, the Commission made clear that gross hedging was appropriate in circumstances where ''net cash positions do not necessarily measure total risk exposure due to differences in the timing of cash commitments, the location of stocks, and differences in grades or types of the cash commodity.'' [441] Thus, the 1977 proposal noted the Commission ''does not intend at this time to alter the provisions of the present definition with respect to the hedging of gross cash position.'' [442] At the time of the 1977 proposal, the ''present definition'' had been promulgated in 1975 by the Administrator of the Commodity Exchange Authority based on the statutory definition; and the Administrator had interpreted the statutory definition to recognize gross hedging as bona fide in the context of a merchant who ''may hedge his fixed-price purchase commitments by selling futures and *at the same time* hedge his fixed-price sale commitments by buying futures,'' rather than hedging only his net position.[443]

*Comments on specific, identifiable risk:* Commenters requested the Commission consider as economically appropriate any derivative position that a business can reasonably demonstrate reduces or mitigates one or more specific, identifiable risks related to individual or aggregated positions or transactions, based on its own business judgment and risk management policies, whether risk is managed enterprise-wide or by legal entity, line of business, or profit center.[444] One commenter disagreed with what it called a ''one-size-fits-all'' risk management paradigm that requires market participants to calculate risk on a consolidated basis because this approach would require commercial entities to build out new systems in order to manage risk this way. The commenter requests that the Commission instead recognize that current risk management tools are used effectively for positions that are below current limits and those tools remain effective above position limit levels as well.[445]

*Commission Reproposal:* The Reproposal declines to assess the bona fides of a position based solely on whether a commercial enterprise can identify any particular cash position within an aggregated person, the risks of which such derivative position offsets. The Commission believes that such an approach would run counter to the aggregation rules in § 150.4 and would permit an enterprise to cherry pick cash market exposures to justify exceeding position limits, with either a long or short derivative position, even though such derivative position increases the enterprise's risk.

The Commission views a derivative position that increases an enterprise's risk as contrary to the plain language of CEA section 4a(c) and the Commission's bona fide hedging definition, which requires that a bona fide hedging position ''is economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise.'' [446]

If a transaction that increases a commercial enterprise's overall risk should be considered a bona fide hedging position, this would result in position limits not applying to certain positions that should be considered speculative. For example, assume an enterprise has entered into only two cash forward transactions and has no inventory. The first cash forward transaction is a purchase contract (for a particular commodity for delivery at a particular later date). The second cash forward transaction is a sales contract (for the same commodity for delivery on the same date as the purchase contract). Under the terms of the cash forward contracts, the enterprise may take delivery on the purchase contract and re-deliver the commodity on the sales contract. Such an enterprise does not have a net cash market position that exposes it to price risk, because it has both purchased and sold the same commodity for delivery on the same date (such as cash forward contracts for the same cargo of Brent crude oil). The enterprise could establish a short derivative position that would offset the risk of the purchase contract; however, that would increase the enterprise's price risk. Alternatively, the enterprise

[435] *See, e.g.,* CL–Olam–59658 at 4–6.

[436] CL–FIA–59595 at 20–21.

[437] CL–Working Group–60947 at 15.

[438] CL–CMC–60950 at 5.

[439] *See, e.g.,* instructions to Form 204.

[440] 42FR 14832 at 14834 (Mar. 16, 1977).

[441] *Id.*

[442] *Id.*

[443] *See,* Letter from Roger R. Kauffman, Adm'r, Commodity Exchange Authority, to Reid Bondurant, Cotton Exchange (Feb. 13, 1959) (emphasis added), cited in CL–Olam–59658 at 5.

[444] *See, e.g.,* CL–API–59694 at 4, CL–IECAssn–59679 at 10–11, CL–APGA–59722 at 9–10, CL–NCFC–59942 at 5, CL–EEI–EPSA–59602 at 15, and CL–EEI-Sup–60386 at 7.

[445] CL–CMC–60950 at 5.

[446] CEA section 4a(c)(2)(A)(ii).

could establish a long derivative position that would offset the risk of the sales contract; however, that would increase the enterprise's price risk. If price risk reduction at the level of the aggregate person is not a requirement of a bona fide hedging position, such an enterprise could establish either a long or short derivative position, at its election, and claim an exemption from position limits for either derivative position, ostensibly as a bona fide hedging position. If either such position could be recognized as bona fide, position limits would simply not apply to such an enterprise's derivative position, even though the enterprise had no price risk exposure to the commodity prior to establishing such derivative position and created price risk exposure to the commodity by establishing the derivative position. Based on the Commission's experience and expertise, it believes that such a result (entering either a long or short derivative position, whichever the market participant elects) simply cannot be recognized as a legitimate risk reduction that should be exempt from position limits; rather, such a position should be considered speculative for purposes of position limits.

The Commission notes that a commercial enterprise that wishes to separately manage its operations, in separate legal entities, may, under the aggregation requirements of § 150.4, establish appropriate firewalls and file a notice for an aggregation exemption, because separate legal entities with appropriate firewalls are treated as separate persons for purposes of position limits. The Commission explained that an aggregation exemption was appropriate in circumstances where the risk of coordinated activity is mitigated by firewalls.[447]

*Comments on processing hedge:* A commenter requested the Commission recognize, as bona fide, a long or short derivative position that offsets either inputs or outputs in a processing operation, based on the business judgment of the commercial enterprise that it might not be an appropriate time to hedge both inputs and outputs, and requested the Commission withdraw the processing hedge example on pages 75836–7 of the 2013 Position Limits Proposal (proposed example 5 in Appendix C to part 150).[448]

*Commission Reproposal:* For the reasons discussed above regarding gross hedging and specific, identifiable risks, the Reproposal does not recognize as a bona fide hedging position a derivative position that offsets either inputs or outputs in a processing operation, absent additional facts and circumstances. The Commission reiterates its view that, as explained in the Commission's 2013 Position Limits Proposal, by way of example, processing by a soybean crush operation or a fuel blending operation may add relatively little value to the price of the input commodity. In such circumstances, it would be economically appropriate for the processor or blender to offset the price risks of both the unfilled anticipated requirement for the input commodity and the unsold anticipated production; such a hedge would, for example, fully lock in the value of soybean crush processing.[449] However, under such circumstances, merely entering an outright derivative position (*i.e.,* either a long position or a short position, at the processor's election) appears to be risk increasing, since the price risk of such outright position appears greater than, and not offsetting of, the price risk of anticipated processing and, thus, such outright position would not be economically appropriate to the reduction of risks.

*Comments on economically appropriate anticipatory hedges:* Commenters requested the Commission recognize derivative positions as economically appropriate to the reduction of certain anticipatory risks, such as irrevocable bids or offers.[450]

*Commission Reproposal:* The Commission has a long history of providing for the recognition, in § 1.3(z)(2), as enumerated bona fide hedging positions, of anticipatory hedges for unfilled anticipated requirements and unsold anticipated production, under the process of § 1.48.[451] The Reproposal continues to enumerate those two anticipatory hedges, along with two new anticipatory hedges for anticipated royalties and contracts for services, as discussed below.

The Commission did not propose an enumerated exemption for binding, irrevocable bids or offers as the Commission believes that an analysis of the facts and circumstances would be necessary prior to recognizing such an exemption. Consequently, the Reproposal does not provide for such an enumerated exemption. However, the Commission withdraws the view that a binding, irrevocable bid or offer fails to meet the economically appropriate test.[452] Rather, the Commission will permit exchanges, under § 150.9, to make a facts-and-circumstances determination as to whether to recognize such and other anticipatory hedges as non-enumerated bona fide hedges, consistent with the Commission's recognition ''that there can be a gradation of probabilities that an anticipated transaction will occur.'' [453]

iii. Change in Value Requirement

*Commission proposal:* To satisfy the change in value requirement, the hedging position must arise from the potential change in the value of: (I) Assets that a person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising; (II) liabilities that a person owes or anticipates incurring; or (III) services that a person provides, purchases, or anticipates providing or purchasing.[454] The proposed definition incorporated the potential change in value requirement in current § 1.3(z)(1).[455] This provision largely mirrors the provision of CEA section 4a(c)(2)(A)(iii).[456]

*Comments on change in value:* One commenter urged a more narrow definition of bona fide hedging that restricts exemptions to ''commercial entities that deal exclusively in the production, processing, refining, storage, transportation, wholesale or retail distribution, or consumption of physical commodities.'' [457] However, numerous commenters urged the Commission to enumerate new exemptions consistent with the change in value requirement, such as for merchandising, as discussed below.

*Commission Reproposal:* The Reproposal retains the change in value requirement as proposed, which mirrors CEA section 4a(c)(2)(A)(iii). Rather than further restrict the types of commercial entities who may avail themselves of a

[447] *See* discussion under section II.B.3 (*Criteria for Aggregation Relief in Rule 150.4(b)(2)(i)*) of the 2016 Final Aggregation Rule.

[448] CL–Cargill–59638 at 2–4.

[449] December 2013 Position Limits Proposal, 78 FR at 75709.

[450] *See, e.g.,* CL–Cargill–59638 at 2–4.

[451] 17 CFR 1.3(z)(2) and 1.48 (2010).

[452] December 2013 Position Limits Proposal, 78 FR at 75720.

[453] *Id.* at 75719.

[454] *Id.* at 75710.

[455] 17 CFR 1.3(z) (2010).

[456] As noted in the December 2013 Position Limits Proposal, 78 FR at 75710, CEA section 4a(c)(2)(A)(iii)(II) uses the phrase ''liabilities that a person owns or anticipates incurring.'' The Commission interprets the word ''owns'' to be a typographical error, and interprets the word ''owns'' to be ''owes.'' A person may owe on a liability, and may anticipate incurring a liability. If a person ''owns'' a liability, such as a debt instrument issued by another, then such person owns an asset. Because assets are included in CEA section 4a(c)(2)(A)(iii)(I), the Commission interprets ''owns'' to be ''owes.''

[457] CL–PMAA–NEFI–60952 at 2.

bona fide hedging exemption under the change in value requirement, the Commission notes that the reproposed definition also reflects the statutory requirement under the temporary substitute test, that the hedging position be a substitute for a position taken or to be taken in a physical marketing channel, either by the market participant or the market participant's pass-through swap counterparty.

*Comments on anticipatory merchandising or storage:* Numerous commenters asserted the Commission should recognize anticipatory merchandising as a bona fide hedge, as included in CEA section 4a(c)(A)(iii), such as (1) a merchant desiring to lock in the price differential between an unfixed price forward commitment and an anticipated offsetting unfixed price forward commitment, where there is a reasonable basis to infer that an offsetting transaction was likely to occur (such as in anticipation of shipping), (2) a bid or offer, where there is a reasonably anticipated risk that such bid or offer will be accepted, or (3) an anticipated purchase and/or anticipated storage of a commodity, prior to anticipated merchandising (or usage).[458]

Commenters recommended the Commission recognize unfilled storage capacity as the basis of a bona fide hedge of, either (1) anticipated rents (*e.g.,* a type of anticipated asset or liability), (2) anticipated merchandising, or (3) anticipated purchase and storage prior to usage.[459] By way of example, one commenter contended anticipated rent on a storage asset is like an option and the appropriate hedge position should be dynamically adjusted.[460] Also by way of example, another commenter suggested enumerated hedges should include (1) offsetting long and short positions in commodity derivative contracts as hedges of storage or transportation of the commodity underlying such contracts; and (2) positions that hedge the value of assets owned, or anticipated to be owned, used to produce, process, store or transport the commodity underlying the derivative.[461]

*Commission Reproposal:* The Commission notes that an exchange, under reproposed § 150.9, as discussed below, is permitted to recognize anticipated merchandising or anticipated purchase and storage, as potential non-enumerated bona fide hedging positions, subject to assessment of the particular facts and circumstances, including such information as the market participant's activities (taken or to be taken) in the physical marketing channel and arrangements for storage facilities. While the Commission previously discussed its doubt that storage hedges generally will meet the economically appropriate test, because the value fluctuations in a calendar month spread in a commodity derivative contract will likely have at best a low correlation with value fluctuations in expected returns (*e.g.,* rents) on unfilled storage capacity,[462] the Commission now withdraws that discussion of doubt and, as reproposed, would review exchange-granted non-enumerated bona fide hedging exemptions for storage with an open mind.

The Commission does not express a view as this time on one commenter's assertion that the anticipated rent on a storage asset is like an option; the commenter did not provide data regarding the relationship between calendar spreads and the ''profitability of filling storage.'' The Commission notes that, under the Reproposal, an exchange could evaluate the particulars of such a situation in an application for a non-enumerated hedging position.

Similarly, as reproposed, an exchange could evaluate the particulars of other situations, such as a commenter's example of storage or transportation hedges. The Commission notes that it is not clear from the comments how the value fluctuations of calendar month or location differentials are related to the fluctuations in value of storage or transportation. Regarding a commenter's examples of assets owned or anticipated to be owned, it is not clear how the value fluctuations of whatever would be the relevant hedging position (*e.g.,* long, short, or calendar month spread) are related to the fluctuations in value of whatever would be the particular assets (*e.g.,* tractors, combines, silos, semi-trucks, rail cars, pipelines) to be used to produce, process, store or transport the commodity underlying the derivative.

*Comments on unfixed price commitments:* Commenters recommended the Commission recognize, as a bona fide hedge, the fixing of the price of an unfixed price commitment, for example, to reduce the merchant's operational risk and potentially to acquire a commodity through the delivery process on a physical-delivery futures contract.[463] Another commenter provided an example of a preference to shift unfixed-price exposure on cash commitments from daily index prices to the first-of-month price under the NYMEX Henry Hub Natural Gas core referenced futures contract.[464] A commenter suggested that the interpretation of a fixed price contract should include ''basis priced contracts which are purchases or sales with the basis value fixed between the buyer and the seller against a prevailing futures'' contract; the commenter noted such basis risk could be hedged with a calendar month spread to lock in their purchase and sale margins.[465] Another commenter requested the Commission explicitly recognize index price transactions as appropriate for a bona fide hedging exemption, citing concerns that the price of an unfixed price forward sales contract may fall below the cost of production.[466]

*Commission Reproposal:* The Commission affirms its belief that a reduction in a price risk is required under the economically appropriate test of CEA section 4a(c)(2)(A)(ii); consistent with the economically appropriate test, a potential change in value (*i.e.,* a price risk) is required under CEA section 4a(c)(2)(A)(iii). In both the reproposed and proposed definitions of bona fide hedging position, the incidental test would require a reduction in price risk. Although the Reproposal deletes the incidental test from the first paragraph of the bona fide hedging position definition (as discussed above), the Commission notes that it interprets risk in the economically appropriate test as price risk, and does not interpret risk to include operational risk. Interpreting risk to include operational risk would broaden the scope of a bona fide hedging position beyond the Commission's historical interpretation

[458] *See, e.g.,* CL–FIA–59595 at 30–31, CL–FIA–60303 at 6, CL–EEI–EPSA–59602 at 17–18, CL–EEI–59945 at 6, CL–CMC–60950 at 6, CL–CMC–60391 at 4–5, CL–CMC–60318 at 5, CL–CMC–59634 at 3, 20–22, CL–Cargill–59638 at 2–4, CL–ADM–59640 at 2–3, CL–Olam–59946 at 4, CL–BG Group–59656 at 10–11, CL–ASCA–59667 at 2, CL–NGSA–60379 at 5, CL–NGSA–59674 at 2, 18–24, CL–Working Group–60383 at 15, CL–Working Group–59937 at 5–6, 10–12, CL–Working Group–59656 at 16–18, 21–23, 26, CL–API–59694 at 5–6, CL–MSCGI–59708 at 2–3, 18–20, CL–CME–59718 at 56–57, 59, CL–Armajaro–59729 at 1, CL–AFBF–59730 at 2, CL–NCFC–59942 at 2–4, CL–ICE–60310 at 4, CL–ICE–60387 at 9, CL–ISDA/SIFMA–59611 at 37–38, CL–COPE–59662 at 15–16, and CL–GSC–59703 at 3–4.

[459] *See, e.g.,* CL–Cargill–59638 at 2–4, CL–CME–59718 at 57–58, CL–NEM–59586 at 4, CL–FIA–59595 32–33, CL–ISDA/SIFMA–59611 at 4, CL–CMC–59634 at 5, CL–LDC–59643 at 2, CL–BG Group-59656 at 10, CL–COPE–59950 at 5, CL–COPE–59662 at 14–15, CL—Working Group–59693 at 23–26, CL–GSC–59703 at 2–3, CL–AFBF–59730 at 2, CL–SEMP–59926 at 6–7, CL–EDF–60398 at 8–9, CL–EDF–59961 at 2–3, CL–Andersons–60256 at 1–3, and CL–SEMP–60384 at 4–5.

[460] CL–ISDA/SIFMA–59611, Annex B at 7.

[461] CL–EEI–EPSA–60925 at 13.

[462] December 2013 Position Limits Proposal, 78 FR at 75718.

[463] *See, e.g.,* CL–Olam–59946 at 4, and CL–NCFC–59942 at 2–4.

[464] CL–NCGA–NGSA–60919 at 4–5.

[465] CL–NGFA–60941 at 4.

[466] CL–NCGA–NGSA–60919 at 5.

and may have adverse impacts that are inconsistent with the policy objectives of limits in CEA section 4a(a)(3)(B).

The Commission has consistently required a bona fide hedging position to be a position that is shown to reduce price risk in the conduct and management of a commercial enterprise.[467] By way of background, the Commission notes, in promulgating the definition of bona fide hedging position in § 1.3(z), it explained that a bona fide hedging position ''must be economically appropriate to risk reduction, such risks must arise from operation of a commercial enterprise, and the price fluctuations of the futures contracts used in the transaction must be substantially related to fluctuations of the cash market value of the assets, liabilities or services being hedged.'' [468] As noted above, the Dodd-Frank Act added CEA section 4a(c)(2), which copied the economically appropriate test from the Commission's definition in § 1.3(z)(1). Thus, the Commission believes it is reasonable to interpret that statutory standard in the context of the Commission's historical interpretation of § 1.3(z).

While the Commission has enumerated a calendar month spread as a bona fide hedge of offsetting unfixed-price cash commodity sales and purchases, the Reproposal will permit an exchange, under reproposed § 150.9, to conduct a facts-and-circumstances, case-by-case review to determine whether a calendar month spread is appropriately recognized as a bona fide hedging position for only a cash commodity purchase *or* sales contract. For example, assume a merchant enters into an unfixed-price sales contract (*e.g.,* priced at a fixed differential to a deferred month futures contract), and immediately enters into a calendar month spread to reduce the risk of the fixed basis moving adversely. It may not be economically appropriate to recognize as bona fide a long futures position in the spot (or nearby) month and a short futures position in a deferred calendar month matching the merchant's cash delivery obligation, in the event the spot (or nearby) month price is higher than the deferred contract month price (referred to as backwardation, and characteristic of a spot cash market with supply shortages), because such a calendar month futures spread would lock in a loss and may be indicative of an attempt to manipulate the spot (or nearby) futures price.

Regarding the risk of an unfixed price forward sales contract falling below the cost of production, the Reproposal enumerates a bona fide hedging exemption for unsold anticipated production; the Commission clarifies, as discussed below, that such an enumerated hedge is available regardless of whether production has been sold forward at an unfixed (that is, index) price.

*Comments on cash and carry:* Commenters requested the Commission enumerate, as a bona fide hedging position, a ''cash and carry'' trade, where a market participant enters a nearby long futures position and a deferred short futures position, with the intention to take delivery and carry the commodity for re-delivery.[469]

*Commission Reproposal:* The Reproposal does not propose to enumerate a cash and carry trade as a bona fide hedging position. A cash and carry trade appears to fail the temporary substitute test, since such market participant is not using the derivative contract as a substitute for a position taken or to be taken in the physical marketing channel. The long futures position in the cash and carry trade is in lieu of a purchase in the cash market. In the 2016 Supplemental Proposal, the Commission asked whether, and subject to what conditions (*e.g.,* potential facilitation of liquidity for a bona fide hedger of inventory), a cash and carry position might be recognized by an exchange as a spread exemption under § 150.10, subject to the Commission's *de novo* review.[470] This issue is discussed under § 150.10, regarding exchange recognition of spread exemptions.

iv. Pass-Through Swap Offsets and Offsets of Hedging Swaps

*Commission proposal:* The Commission proposed to recognize as bona fide a commodity derivative contract that reduces the risk of a position resulting from a swap executed opposite a counterparty for which the position at the time of the transaction would qualify as a bona fide hedging position.[471] This proposal mirrors the requirements in CEA section 4a(c)(B)(i). The proposal also clarified that the swap itself is a bona fide hedging position to the extent it is offset. However, the Commission proposed that it would not recognize as bona fide hedges an offset in physical-delivery contracts during the shorter of the last five days of trading or the time period for the spot month in such physical-delivery commodity derivative contract (the ''five-day'' rule, discussed further below).

*Comments received:* As noted above, commenters recommended that the Commission's bona fide hedging definition should reflect the standards in CEA section 4a(c). One commenter suggested that the Commission broaden the pass-through swap offset provisions to accommodate secondary pass-through transactions among affiliates within a corporate organization to make ''the most efficient and effective use of their existing corporate structures.'' [472]

*Commission Reproposal:* The Commission agrees that the bona fide hedging definition, in general, and the pass-through swap provision, in particular, should more closely reflect the statutory standards in CEA section 4a(c). Under the proposed definition, a market participant who reduced the risk of a swap, where such swap was a bona fide hedging position for that market participant, would not have received recognition for the swap offset as a bona fide hedging position, as this provision in CEA section 4a(c)(2)(B)(ii) was not mirrored in the proposed definition.[473] To adhere more closely to the statutory standards, the Reproposal recognizes such offset as a bona fide hedging position. Consistent with the proposal for offset of a pass-through swap, the Reproposal imposes a five-day rule restriction on the offset in a physical-delivery contract of a swap used as a bona fide hedge; however, as reproposed, an exchange listing a physical-delivery contract may recognize, on a case-by-case basis, such offset as a non-enumerated bona fide hedging position pursuant to the process in reproposed § 150.9.

The Reproposal retains and clarifies in subparagraph (ii)(A) that the bona fides of a pass-through swap may be

[467] The Commission distinguishes operational risk, which may arise from a potential failure of a counterparty to a cash market forward transaction, from price risks in the conduct and management of a commercial enterprise.

[468] 42 FR 14832 at 14833 (March 16, 1977) (proposed definition). The Commission also adopted the incidental test (requiring that the ''purpose is to offset price risks incidental to commercial cash or spot operations''). 42 FR 42748 at 42751 (Aug. 24, 1977) (final definition). Previously, the Secretary of Agriculture promulgated a definition of bona fide hedging position that required a purpose ''to offset price risks incidental to commercial cash or spot operations.'' 40 FR 11560 at 11561 (Mar. 12, 1975).

[469] *See, e.g.,* CL–Armajaro–59729 at 2.

[470] 2016 Supplemental Position Limits Proposal, 81 FR at 38479.

[471] December 2013 Position Limits Proposal, 78 FR at 75710.

[472] CL–NCGA–NGSA–60919 at 8–9.

[473] For example, assume a market participant entered a swap as a bona fide hedging position and, subsequently, offset (that is, lifted) that hedge using a futures contract. The Commission's original proposal would not have recognized the lifting of the hedge as a bona fide hedging transaction, although the statute does.

determined at the time of the transaction by the intermediary. The clarification is intended to reduce the burden on such intermediary of otherwise needing to confirm the continued bona fides of its counterparty over the life of the pass-through swap.

In addition, the Reproposal retains, as proposed, application of the five-day rule to pass-through swap offsets in a physical-delivery contract. However, the Commission notes that under the Reproposal, an exchange listing a physical-delivery contract may recognize, on a case-by-case basis, a pass-through swap offset (in addition to the offset of a swap used as a bona fide hedge), during the last five days of trading in a spot month, as a non-enumerated bona fide hedge pursuant to the process in reproposed § 150.9.

Further, the Reproposal retains the recognition of a pass-through swap itself that is offset, not just the offsetting position (and, thus, permitting the intermediary to exclude such pass-through swap from position limits, in addition to excluding the offsetting position).

Regarding the request to broaden the pass-through swap offset provisions to accommodate secondary pass-through transactions among affiliates, the Commission declines in this Reproposal to broaden the pass-through swap offset exemption beyond the provisions in CEA section 4a(c)(2)(B)(i). However, the Commission notes that a group of affiliates under common ownership is required to aggregate positions under the Commission's requirements in § 150.4, absent an applicable aggregation exemption. In the circumstance of aggregation of positions, recognition of a secondary pass-through swap transaction would not be necessary among such an aggregated group, because the group is treated as one person for purposes of position limits.

v. Additional Requirements for Enumeration or Other Recognition

*Commission proposal:* In 2013, the Commission proposed in subparagraph (2)(i)(D) of the definition of a bona fide hedging position, that, in addition to satisfying the general definition of a bona fide hedging position, a position would not be recognized as bona fide unless it was enumerated in paragraph (3), (4), or (5)(discussed below), or recognized as a pass-through swap offset or pass-through swap.[474] In 2016, in response to comments on the 2013 proposed definition, the Commission proposed, in subparagraph (2)(i)(D)(2) of the definition, to also recognize as bona fide any position that has been otherwise recognized as a non-enumerated bona fide hedging position by either a designated contract market or a swap execution facility, each in accordance with § 150.9(a), or by the Commission.[475]

*Comments received:* Commenters objected to the requirement for a position to be specifically enumerated in order to be recognized as bona fide, noting that the enumerated requirement is not supported by the legislative history of the Dodd-Frank Act, conflicts with longstanding Commission practice and precedent, and may be overly restrictive due to the limited set of specific enumerated hedges.[476] Other commenters recommended that the Commission expand the list of enumerated bona fide hedge positions, to encompass all transactions that reduce risks in the conduct and management of a commercial enterprise, such as anticipatory merchandising hedges and other general examples.[477]

*Commission Reproposal:* In response to comments, the Reproposal retains, as proposed in 2016, a proposed definition that recognizes as bona fide, in addition to enumerated positions, any position that has been otherwise recognized as a non-enumerated bona fide hedging position by either a designated contract market or a swap execution facility, each in accordance with reproposed § 150.9(a), or by the Commission. These provisions for recognition of non-enumerated positions are included in re-designated subparagraph (2)(iii)(C) of the reproposed definition of a bona fide hedging position.

The Commission notes that it is not possible to list all positions that would meet the general definition of a bona fide hedging position. However, the Commission observes that the commenters' many general examples, which they recommended be included in the list of enumerated bona fide hedging positions, generally did not provide sufficient context or facts and circumstances to permit the Commission to evaluate whether recognition as a non-enumerated bona fide hedging position would be warranted. Context would be supplied, for instance, by the provision of the particular market participant's historical activities in the physical marketing channel and such participant's estimate, in good faith, of its reasonably expected activities to be taken in the physical marketing channel.

In a clarifying change, the Commission notes that the Reproposal has re-designated the provisions proposed in subparagraph (2)(i)(D), in new subparagraph 2(iii), regarding the additional requirements for recognition of a position in a physical commodity contract as a bona fide hedging position. Concurrent with this re-designation, the Commission notes the Reproposal re-organizes, also for clarity, the application of the five-day rule to pass-through swaps and hedging swaps in subparagraph (2)(iii)(B), as discussed above.[478]

3. Enumerated Hedging Positions

a. Proposed Enumerated Hedges

In paragraph (3) of the proposed definition of a bona fide hedging position, the Commission proposed four enumerated hedging positions: (i) Hedges of inventory and cash commodity purchase contracts; (ii) hedges of cash commodity sales contracts; (iii) hedges of unfilled anticipated requirements; and (iv) hedges by agents.[479]

*Comments received:* Numerous commenters objected to the provision in proposed subparagraph (3)(iii)(A) that would have limited recognition of a hedge for unfilled anticipated requirements to one year for agricultural commodities. For example, commenters noted a need to hedge unfilled anticipated requirements for sugar for a time period longer than twelve months.[480] Similarly, other commenters noted there may be a need to offset risks arising from investments in processing capacity in agricultural commodities for a period in excess of twelve months.[481]

Other commenters recommended the Commission (1) remove the restriction that unfilled anticipated requirement hedges by a utility be ''required or encouraged to hedge by its public utility commission'' because most public utility commissions do not require or encourage such hedging, (2) expand the reach beyond utilities, by including

[474] December 2013 Position Limits Proposal, 78 FR at 75711.

[475] 2016 Supplemental Position Limits Proposal, 81 FR at 38505.

[476] *See, e.g.,* CL–CME–59718 at 47–53, and CL–BG Group–59656 at 9.

[477] *See, e.g.,* CL–FIA–59595 at 32, CL–FIA–60303 at 6, CL–API–60939 at 3, CL–AGA–60943 at 4, CL–CMC–60950 at 6–9, CL–EEI–EPSA–60925 at 13, and CL–FIA–60937 at 5 and 21.

[478] However, as noted above, as reproposed, an exchange listing a physical-delivery contract may recognize, on a case-by-case basis, a pass-through swap offset, or the offset of a swap used as a bona fide hedge, during the last five days of trading in a spot month, as a non-enumerated bona fide hedge pursuant to the process in reproposed § 150.9.

[479] December 2013 Position Limits Proposal, 78 FR at 75713.

[480] *See, e.g.,* Ex Parte No-869, notes of Feb. 25, 2015 ex parte meeting with The Hershey Company, The J.M. Smucker Co., Louis Dreyfus Commodities, Noble Americans Corp., *et al.*

[481] *See, e.g.,* CL–NGFA–60941 at 8.

entities designated as providers of last resort who serve the same role as utilities, and (3) clarify the meaning of unfilled anticipated requirements, consistent with CFTC Staff Letter No. 12–07.[482]

*Commission Reproposal:* The Reproposal retains the enumerated exemptions as proposed, with two amendments. First, the Commission agrees with the commenters' request to remove the twelve month constraint on hedging unfilled anticipated requirements for agricultural commodities, as that provision appears no longer to be a necessary prudential constraint. Second, the Commission agrees with the commenters' request to remove the condition that a utility be ''required or encouraged to hedge by its public utility commission.'' Accordingly, the condition that a utility be ''required or encouraged to hedge by its public utility commission'' is omitted from the reproposed definition. The Commission notes that under the Reproposal, a market participant, who is not a utility, may request that an exchange consider recognizing a non-enumerated exemption, as it is not clear who would be appropriately identified as a ''provider of last resort'' and under what circumstance such person would reasonably estimate its unfilled requirements.

Consistent with CFTC Staff Letter No. 12–07, the Commission affirms its belief that unfilled anticipated requirements are those anticipated inputs that are estimated in good faith and that have not been filled. Under the Reproposal, an anticipated requirement may be filled, for example, by fixed-price purchase commitments, holdings of commodity inventory by the market participant, or unsold anticipated production of the market participant. However, an unfixed-price purchase commitment does not fill an anticipated requirement, in that the market participant's price risk to the input has not been fixed.

b. Proposed Other Enumerated Hedges Subject to the Five-Day Rule

In paragraph (4) of the proposed definition of a bona fide hedging position, the Commission proposed four other enumerated hedging positions: (i) Hedges of unsold anticipated production; (ii) hedges of offsetting unfixed-price cash commodity sales and purchases; (iii) hedges of anticipated royalties; and (iv) hedges of services.[483] The Commission proposed to apply the five-day rule to all such positions.

*Comments received on the five-day rule:* Numerous commenters requested that the five-day rule be removed from the Commission's other enumerated bona fide hedging positions, as that condition is not included in CEA section 4a(c).

*Commission Reproposal on the five-day rule:* The Commission is retaining the prudential condition of the five-day rule in the other enumerated hedging positions. The Commission has a long history of applying the five-day rule, in its legacy agricultural federal position limits, to hedges of unsold anticipated production and hedges of offsetting unfixed-price cash commodity sales and purchases. However, as discussed in relation to reproposed § 150.9, the Commission will permit an exchange, in effect, to remove the five-day rule on a case-by-case basis in physical-delivery contracts, as a non-enumerated bona fide hedging position, by applying the exchange's experience and expertise in protecting its own physical-delivery market.

*Comments on other enumerated exemptions:* As noted above, commenters recommended removing the twelve-month limitation on agricultural production, as unnecessarily short in comparison to the expected life of investment in production facilities.[484]

*Commission Reproposal on other enumerated exemptions:* The Reproposal removes the twelve-month limitations on unsold anticipated agricultural production and hedges of services for agricultural commodities. As noted above, that provision appears no longer to be a necessary prudential constraint. Otherwise, the Reproposal retains the other enumerated exemptions, as proposed.

c. Proposed Cross-Commodity Hedges

In paragraph (5) of the proposed definition of a bona fide hedging position, the Commission proposed to recognize as bona fide cross-commodity hedges.[485] Cross-commodity hedging would be conditioned on: (i) The fluctuations in value of the position in the commodity derivate contract (or the commodity underlying the commodity derivative contract) being substantially related to the fluctuations in value of the actual or anticipated cash position or pass-through swap (the substantially related test); and (ii) the five-day rule being applied to positions in any physical-delivery commodity derivative contract. The Commission proposed a non-exclusive safe harbor for cross-commodity hedges that would have two factors: A qualitative factor; and a quantitative factor.

*Comments on cross-commodity hedges:* Numerous commenters requested the Commission withdraw the safe harbor quantitative ''test,'' and noted such test is impracticable where there is no relevant cash market price series for the commodity being hedged.[486] Some commenters requested the Commission retain a qualitative approach to assessing whether the fluctuations in value of the position in the commodity derivate contract are substantially related to the fluctuations in value of the actual or anticipated cash position.

One commenter urged the Commission to clarify that market participants need not treat as enumerated cross-commodity hedges strategies where the cash position being hedged is the same cash commodity as the commodity underlying the futures contract even if the cash commodity is not deliverable against the contract. The commenter believes that this clarification would verify that non-deliverable grades of certain commodities could be deemed as the same cash commodity and thus not be deemed a cross-commodity hedge subject to the five-day rule.[487]

Commenters requested the Commission not apply a five-day rule to cross-commodity hedges or, alternatively, permit exchanges to determine the appropriate facts and circumstances where a market participant may be permitted to hold such positions into the spot month,

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[482] *See, e.g.,* CL–Working Group–59693 at 27–28, CL–EEI–EPSA–55953 at 19. CFTC Staff Letter No. 12–07 notes that unfilled anticipated requirements may be recognized as the basis of a bona fide hedging position or transaction under Commission Regulation 151.5(a)(2)(ii)(C) when a commercial enterprise has entered into long-term, unfixed-price supply or requirements contracts as the price risk of such ''unfilled'' anticipated requirements is not offset by an unfixed price forward contract as the price risk remains with the commercial, even though the commercial enterprise has contractually assured a supply of the commodity. Instead, the price risk continues until the forward contract's price is fixed; once the price is fixed on the supply contract, the commercial enterprise no longer has price risk and the derivative position, to the extent the position is above an applicable speculative position limit, must be liquidated in an orderly manner in accordance with sound commercial practices.

[483] December 2013 Position Limits Proposal, 78 FR at 75714.

[484] *See, e.g.,* CL–NGFA–60941 at 8.

[485] December 2013 Position Limits Proposal, 78 FR at 75716.

[486] *See, e.g.,* CL–ICE–60929 at 16, CL–NCGA–NGSA–60919 at 6–7, CL–NCFC–60930 at 2–3, CL–API–60939 at 2, CL–NGFA–60941 at 8, CL–EEI–EPSA–60925 at 10, and CL–IECAssn–60949 at 5–7.

[487] CL–CME–60926 at 6.

noting that a cross-commodity hedge in a physical-delivery contract may be the best hedge of its commercial exposure.[488]

*Commission Reproposal:* The Reproposal retains the cross-commodity hedge provision in paragraph (5) of the definition of a bona fide hedging position as proposed. However, for the reasons requested by commenters and because of confusion regarding application of a safe harbor, the Reproposal does not include the safe harbor quantitative test. If questions arise regarding the bona fides of a particular cross-commodity hedge, it would, as reproposed, be reviewed based on facts and circumstances, including a market participant's qualitative review of a particular cross-commodity hedge.

The Reproposal retains the five-day rule, because a market participant who is hedging the price risk of a non-deliverable cash commodity has no need to make or take delivery on a physical-delivery contract. However, the Commission notes that an exchange may consider, on a case-by-case basis in physical-delivery contracts, whether to recognize such cross-commodity positions as non-enumerated bona fide hedges during the shorter of the last five days of trading or the time period for the spot month, by applying the exchange's experience and expertise in protecting its own physical-delivery market, under the process of § 150.9.

4. Commodity Trade Options Deemed Cash Equivalents

*Commission proposal:* The Commission requested comment as to whether the Commission should use its exemptive authority under CEA section 4a(a)(7) to provide that the offeree of a commodity option would be presumed to be a pass-through swap counterparty for purposes of the offeror of the trade option qualifying for the pass-through swap offset exemption.[489] Alternatively, the Commission, noting that forward contracts may serve as the basis of a bona fide hedging position exemption, proposed that it may similarly include trade options as one of the enumerated bona fide hedging exemptions. The Commission noted, for example, such an exemption could be similar to the enumerated exemption for the offset of the risk of a fixed-price forward contract with a short futures position.

*Comments on trade option exemptions:* Commenters requested that the Commission clarify that hedges of commodity trade options be recognized as bona fide hedges, as would be available for other cash positions.[490]

*Commission Reproposal:* The Commission agrees with the commenters and has determined to address the request that commodity trade options should be recognized as the basis for a bona fide hedging position, as would be available for other cash positions. The reproposed definition of a bona fide hedging position adds new paragraph (6), specifying that a commodity trade option meeting the requirements of § 32.3 may be deemed a cash commodity purchase or sales contract, as the case may be, provided that such option is adjusted on a futures-equivalent basis. The reproposed definition also provides non-exclusive guidance on making futures-equivalent adjustments to a commodity trade option. For example, the guidance provides that the holder of a trade option, who has the right, but not the obligation, to call the commodity at a fixed price, may deem that trade option, converted on a futures-equivalent basis, to be a position in a cash commodity purchase contract, for purposes of showing that the offset of such cash commodity purchase contract is a bona fide hedging position.

Because the price risk of an option, including a trade option with a fixed strike price, should be measured on a futures-equivalent basis,[491] the Commission has determined that under the reproposed definition, a trade option should be deemed equivalent to a cash commodity purchase or sales contract only if adjusted on a futures-equivalent basis. The Commission notes that it may not be possible to compute a futures-equivalent basis for a trade option that does not have a fixed strike price. Thus, under the reproposed definition, a market participant may not use a trade option as a basis for a bona fide hedging position until a fixed strike price reasonably may be determined.

5. App. C to Part 150—Examples of Bona Fide Hedging Positions for Physical Commodities

*Commission proposal:* The Commission proposed a non-exhaustive list of examples meeting the requirements of the proposed definition of a bona fide hedging position, noting that market participants could see whether their practices fall within the list.[492]

*Comments on examples:* Comments regarding the processing hedge example number 5 of proposed Appendix C to part 150 are discussed above. Another commenter requested the Commission affirm that aggregation is required pursuant to an express or implied agreement when that agreement is to trade referenced contracts, and that aggregation is not triggered by the condition in example number 7 of proposed Appendix C to part 150, where a Sovereign grants an option to a farmer at no cost, conditioned on the farmer entering into a fixed-price forward sale.[493]

*Commission Reproposal:* The Commission agrees with the commenter that aggregation is required pursuant to an express or implied agreement when that agreement is to trade referenced contracts. Proposed example number 7 was focused on recognizing the legitimate public policy objectives of a sovereign furthering the development of a cash spot and forward market in agricultural commodities. To avoid confusion regarding the aggregation policy under rule 150.4, in the Reproposal, the Commission has revised example number 7, and has provided an interpretation that a farmer's synthetic position of a long put option may be deemed a pass-through swap, for purposes of a sovereign who has granted a cash-settled call option at no cost to such farmer in furtherance of a public policy objective to induce such farmer to sell production in the cash market. The Commission notes the combination of a farmer's forward sale agreement and a granted call option is approximately equivalent to a purchased put option. A farmer anticipating production or holding inventory may use such a long position in a put option as a bona fide hedging position.

The Reproposal also includes a number of conforming amendments and corrections of typographical errors. Specifically, it conforms example number 4 regarding a utility to the

[488] *See, e.g.,* CL–FIA–60937 at 22, CL–CCI–60935 at 8–9.

[489] December 2013 Position Limits Proposal, 78 FR at 75711. The Commission also requested comment on whether it would be appropriate to exclude commodity trade options from the definition of referenced contract. As discussed above, the Commission has determined to exclude trade options from the definition of referenced contract. Previous to this reproposed rule, the Commission observed that federal position limits should not apply to trade options. 81 FR 14966 at 14971 (Mar. 21, 2016).

[490] *See, e.g.,* CL–EEI–EPSA–60925 at 15.

[491] *See* the discussion of the definition of futures-equivalent in reproposed § 150.1, above.

[492] December 2013 Position Limits Proposal, 78 FR at 75739, 75828.

[493] CL–FIA–59595 at 35, CL–FIA–59566 at 3–7, citing December 2013 Position Limits Proposal, 78 FR at 75837.

changes to paragraph (3)(iii)(B) of the bona fide hedging position definition, as discussed above. The references in the examples to a 12-month restriction on hedges of agricultural commodities have also been removed because the Reproposal eliminates those proposed restrictions from the reproposed enumerated bona fide hedging positions, as discussed above. In addition, based on discussions with cotton merchants, example number 6, regarding agent hedging, has been amended from a generic example to a specific illustration of the hedge of cotton equities purchased by a cotton merchant from a producer, under the USDA loan program. Finally, the Reproposal corrects typographical errors in example number 12, regarding the hedge of copper inventory and the cross-hedge of copper wire inventory, to correctly reflect the 25,000 pound unit of trading in the Copper core referenced futures contract, and deletes the unnecessary reference to the price relationship between the nearby and deferred Copper futures contracts.

*B. § 150.2—Position Limits*

1. Setting Levels of Spot Month Limits

In the December 2013 Position Limits Proposal, the Commission proposed to establish speculative position limits on 28 core referenced futures contracts in physical commodities.[494]

As stated in the December 2013 Position Limits Proposal, the Commission proposed to set the initial spot month position limit levels for referenced contracts at the existing DCM-set levels for the core referenced futures contracts because the Commission believed this approach to be consistent with the regulatory objectives of the Dodd-Frank Act amendments to the CEA and many market participants are already used to those levels.[495] The Commission also stated that it was considering setting initial spot month limits based on estimated deliverable supplies submitted by CME Group Inc. (''CME'') in 2013.[496] The Commission suggested that it might use the exchange's estimated deliverable supplies if it could verify that they are reasonable.[497] The Commission further stated that it was considering another alternative of using, in the Commission's discretion, the recommended level, if any, of the spot month limit as submitted by each DCM listing a core referenced futures contract (if lower than 25 percent of estimated deliverable supply).[498]

2. Verification of Estimated Deliverable Supply

The Commission received comment letters from CME, Intercontinental Exchange (''ICE'') and Minneapolis Grain Exchange, Inc. (''MGEX'') containing estimates of deliverable supply. CME submitted updated estimates of deliverable supply for CBOT Corn (C), Oats (O), Rough Rice (RR), Soybeans (S), Soybean Meal (SM), Soybean Oil (SO), Wheat (W), and KC HRW Wheat (KW); COMEX Gold (GC), Silver (SI), Platinum (PL), Palladium (PA), and Copper (HG); NYMEX Natural Gas (NG), Light Sweet Crude Oil (CL), NY Harbor ULSD (HO), and RBOB Gasoline (RB).[499] ICE submitted estimates of deliverable supply for Cocoa (CC), Coffee C (KC), Cotton No. 2 (CT), FCOJ–A (OJ), Sugar No. 11 (SB), and Sugar No. 16 (SF).[500] MGEX submitted an estimate of deliverable supply for Hard Red Spring Wheat (MWE).[501]

The Commission is verifying that the estimates for C, O, RR, S, SM, SO, W, and KW submitted by CME are reasonable. The Commission is verifying that the estimate for MWE submitted by MGEX is reasonable. The Commission is verifying that the estimates for CC, KC, CT, OJ, SB, and SF submitted by ICE are reasonable. The Commission is verifying that the estimates for GC, SI, PL, PA, and HG submitted by CME are reasonable. Finally, the Commission is verifying that the estimates for NG, CL, HO, and RB submitted by CME are reasonable. In verifying that all of these estimates of deliverable supply are reasonable, Commission staff reviewed the exchange submissions and conducted its own research. Commission staff reviewed the data submitted, confirmed that the data submitted accurately reflected the source data, and considered whether the data sources were authoritative. Commission staff considered whether the assumptions made by the exchanges in the submissions were acceptable, or whether alternative assumptions would lead to similar results. In response to Commission staff questions about the exchange submissions, the Commission received revised estimates from exchanges. In some cases, Commission staff conducted trade source interviews. Commission staff replicated the calculations included in the submissions.

[494] *See generally* December 2013 Position Limits Proposal, 78 FR at 75725. The 28 core referenced futures contracts for which initial limit levels were proposed are: Chicago Board of Trade (''CBOT'') Corn, Oats, Rough Rice, Soybeans, Soybean Meal, Soybean Oil and Wheat; Chicago Mercantile Exchange Feeder Cattle, Lean Hog, Live Cattle and Class III Milk; Commodity Exchange, Inc., Gold, Silver and Copper; ICE Futures U.S. Cocoa, Coffee C, FCOJ–A, Cotton No. 2, Sugar No. 11 and Sugar No. 16; Kansas City Board of Trade Hard Winter Wheat (on September 6, 2013, CBOT and the Kansas City Board of Trade (''KCBT'') requested that the Commission permit the transfer to CBOT, effective December 9, of all contracts listed on the KCBT, and all associated open interest); Minneapolis Grain Exchange Hard Red Spring Wheat; and New York Mercantile Exchange (''NYMEX'') Palladium, Platinum, Light Sweet Crude Oil, NY Harbor ULSD, RBOB Gasoline and Henry Hub Natural Gas.

[495] December 2013 Position Limits Proposal, 78 FR at 75727. Several commenters supported establishing the initial levels of spot month speculative position limit levels at the levels then established by DCMs and listed in Appendix D to part 150, December 2013 Position Limits Proposal, 78 FR at 75739–40 (generally stating that the then current levels are high enough and raising them could cause problems with contract performance. *E.g.,* CL–WGC–59558 at 1–2; CL–Sen. Levin–59637 at 7; CL–AFBF–59730 at 3; CL–NGFA–59956 at 2; CL–NGFA–60312 at 3; CL–NCBA–59624 at 3; CL–Bakers–59691 at 1. Several commenters expressed the view that DCMs are best able to determine appropriate spot month limits and the Commission should defer to their expertise. *E.g.,* CL–NCBA–59624 at 3; CL–Cactus–59660 at 3; CL–TCFA–59680 at 3; CL–NGFA–59610 at 2; CL–MGEX–59635 at 2; CL–MGEX–59932 at 2; CL–MGEX–60380 at 1; CL–ICE–60311 at 1; CL–Thornton–59729 at 1.

[496] December 2013 Position Limits Proposal, 78 FR at 75727. The CME July 1, 2013 deliverable supply estimates are available on the Commission's Web site at *http://www.cftc.gov/idc/groups/public/@swaps/documents/file/cmegroupdeliverable070113.pdf; see also* December 2013 Position Limits Proposal, 78 FR at 75727, n. 406. Several commenters supported using the alternative level of spot-month position limits based on CME's deliverable supply estimates as listed in Table 9 of the December 2013 Position Limits Proposal, generally stating that the alternative estimates are more up to date than the deliverable supply estimates underlying the spot month speculative position limits currently established by the DCMs, and therefore more appropriate for use in setting federal limits. *E.g.,* CL–FIA–59595 at 3, 8; CL–EEI–EPSA–59602 at 9; CL–CMC–59634 at 14; CL–Olam–59658 at 1, 3; CL–BG Group–59656 at 6; CL–COPE–59662 at 21; CL–Calpine–59663 at 3; CL–NGSA–59673 at 37; CL–NGSA–59900 at 11; CL–Working Group–59693 at 58–59; CL–CME–60406 at 2–3 and App. A; CL–CME–60307 at 4; CL–CME–59718 at 3, 20–23; CL–Sempra–59926 at 3–4; CL–BG Group–59937 at 2–3; CL–EPSA–59953 at 2–3; CL–ICE–59966 at 5–6; CL–ICE–59962 at 5; CL–US Dairy–59597 at 4; CL–Rice Dairy–59601 at 1; CL–NMPF–59652 at 4; CL–FCS–59675 at 5.

[497] December 2013 Position Limits Proposal, 78 FR at 75727. The U.S. Chamber of Commerce's Center for Capital Markets Competitiveness commented that the CFTC must update estimates of deliverable supply, rather than relying on existing exchange-set spot month limit levels. CL–Chamber–59684 at 6–7.

[498] December 2013 Position Limits Proposal, 78 FR at 75728.

[499] CL–CME–61007 at 5. *See also* CL–CME–61011; CL–CME–61012; CL–CME–60785 (earlier submission of deliverable supply estimates); CL–CME–60435 (earlier submission of deliverable supply estimates); CL–CME–60406 (earlier submission of deliverable supply estimates). The Commission did not receive an estimate for Live Cattle (LC).

[500] CL–ICE–60786. ICE also submitted an estimate for Henry Hub natural gas. CL–ICE–60684.

[501] CL–MGEX–61038 at Exhibit A; *see also* CL–MGEX–60938 at 2 (earlier submission of deliverable supply estimate).

In verifying the exchange estimates of deliverable supply, the Commission is not endorsing any particular methodology for estimating deliverable supply beyond what is already set forth in Appendix C to part 38 of the Commission's regulations.[502] As circumstances change over time, exchanges may need to adjust the methodology, assumptions and allowances that they use to estimate deliverable supply to reflect then current market conditions and other relevant factors. The Commission anticipates that it will base initial spot-month position limits on the current verified exchange estimates as and to the extent described below, unless an exchange provides additional updates during the Reproposal comment period that the Commission can verify as reasonable.

3. Single-Month and All-Months-Combined Limits

*Commission Proposal:* In the December 2013 Position Limits Proposal, the Commission proposed to set the level of single-month and all-months-combined limits (collectively, non-spot month limits) based on total open interest for all referenced contracts in a commodity.[503] The Commission also proposed to estimate average open interest based on the largest annual average open interest computed for each of the past two calendar years, using either month-end open contracts or open contracts for each business day in the time period, as the Commission finds in its discretion to be reliable.[504] For setting the levels of initial non-spot month limits, the Commission proposed to use open interest for calendar years 2011 and 2012 in futures contracts, options thereon, and in swaps that are significant price discovery contracts that are traded on exempt commercial markets.[505] The Commission explained that it had reviewed preliminary data submitted to it under part 20, but preliminarily decided not to use it for purposes of setting the initial levels of single-month and all-months-combined position limits because the data prior to January 2013 was less reliable than data submitted later.[506] The Commission noted that it was considering using part 20 data, should it determine such data to be reliable, in order to establish higher initial levels in a final rule.[507]

In the June 2016 Supplemental Proposal, the Commission noted that, since the December 2013 Position Limits Proposal, the Commission worked with industry to improve the quality of swap position data reported to the Commission under part 20.[508] The Commission also noted that, in light of the improved quality of such swap position data reporting, the Commission intended to rely on part 20 swap position data, given adjustments for obvious errors (*e.g.,* data reported based on a unit of measure, such as an ounce, rather than a futures-equivalent number of contracts), to establish initial levels of federal non-spot month limits on futures and swaps in a final rule.

*Comments Received:* Commenters requested that the Commission delay the imposition of hard non-spot month limits until it has collected and evaluated complete open interest data.[509]

*Commission Reproposal:* The Commission has determined that certain part 20 large trader position data, after processing and editing by Commission staff as described below,[510] is reliable. The Commission has determined to repropose the initial non-spot month position limit levels based on the combination of such adjusted part 20 swaps data and data on open interest in physical commodity futures and options from the relevant exchanges, as described below. The Commission is using two 12-month periods of data, covering a total of 24 months, rather than two calendar years of data, as is practicable, in reproposing the initial non-spot month position limit levels.

Data Editing

Commission staff analyzed and evaluated the quality of part 20 data for the period from July 1, 2014 through June 30, 2015 (''Year 1''), and the period from July 1, 2015 through June 30, 2016 (''Year 2'').[511] The Commission used open contracts as reported for each business day in the time periods, rather than month-end open contracts, primarily because it lessens the impact of missing data. Averaging generally also smooths over errors in reporting when there is both under- and over-reporting, both of which the Commission observed in the part 20 data. By calculating a daily average for each month for each reporting entity,[512] one calculates a reporting entity's open contracts on a ''representative day'' for each month. The Commission then summed the open contracts for each reporting entity on this representative day, to determine the average open interest for a particular month.[513]

First, for each of Year 1 and Year 2, Commission staff identified all reported positions in swaps that do not satisfy the definition of referenced contract as proposed in the December 2013 Position Limits Proposal[514] and removed those positions from the data set. For example, swaps settled using the price of the LME Gold PM Fix contract do not meet the definition of referenced contract for the gold core referenced futures contract (GC) but positions reported based on these types of swaps represented 14% of records submitted

[502] 17 CFR part 38, Appendix C.

[503] December 2013 Position Limits Proposal, 78 FR at 75729. The Commission currently sets the single-month and all-months-combined limits based on total open interest for a particular commodity futures contract and options on that futures contract, on a futures-equivalent basis.

[504] December 2013 Position Limits Proposal, 78 FR at 75730.

[505] *Id.*

[506] December 2013 Position Limits Proposal, 78 FR at 75733. Thus, the initial levels as proposed in the December 2013 Position Limits Proposal represented the lower bounds for the initial levels that the Commission would establish in final rules.

[507] December 2013 Position Limits Proposal, 78 FR at 75734. The Commission also stated that it was considering using data from swap data repositories, as practicable. *Id.* The Commission has determined that it is not yet practicable to use data from swap data repositories.

[508] 2016 Supplemental Position Limits Proposal, 81 FR at 38459.

[509] *E.g.,* CL–FIA–59595 at 3, 14; CL–EEI–EPSA–59602 at 10–11; CL–MFA–60385 at 4–7; CL–MFA–59606 at 22–23; CL–ISDA/SIFMA–59611 at 28–29; CL–CMC–59634 at 13; CL–Olam–59658 at 3; CL–COPE–59662 at 22; CL–Calpine–59663 at 4; CL–CCMC–59684 at 4–5; CL–NFP–59690 at 20; CL–Just Energy–59692 at 4; CL–Working Group–59693 at 62.

[510] Where relevant and practicable, Commission staff consulted and followed the Office of Management and Budget Standards and Guidelines for Statistical Surveys, September 2006, available at *https://www.whitehouse.gov/sites/default/files/omb/inforeg/statpolicy/standards_stat_surveys.pdf.*

[511] There is no part 20 swaps data for Sugar No. 16 (SF).

[512] A reporting entity is a clearing member or a swap dealer required to report large trader position data for physical commodity swaps, as defined in 17 CFR 20.1.

[513] Because there may be missing data, using open contracts for each business day in the time period that a reporting entity submits a report may overestimate open interest, compared to taking a straight average of the open contracts over all business days in the time period. However, the Commission believes it is reasonable to assume that the open position in swaps for a reporting entity failing to report for a particular business day is more accurately reflected by that reporting entity's average reported open swaps for the month, rather than zero. Hence, in choosing this approach, the Commission chooses to repropose higher non-spot month limit levels.

[514] This adjustment may have removed fewer than all of the reported positions in swaps that do not satisfy the definition of referenced contract as adopted, and therefore may have resulted in a higher level of open interest (which would result in a higher limit level). For instance, swaps reported under part 20 include trade options, and the Commission is reproposing an amended definition of ''referenced contract'' to expressly exclude trade options. *See* the discussion of the defined term ''referenced contract'' under § 150.1, above. Because part 20 does not require trade options to be identified, the Commission could not exclude records of trade options from open interest or position size.

under part 20 by reporting entities for gold swaps. The percentage of average daily open interest excluded from the adjusted part 20 swaps data resulting from this deletion are set forth in Table 1 below. Other adjustments to the data are described below. Because not all commodities required exclusion of non-referenced contracts, the Commission reports only the 11 commodities that required this type of exclusion.

TABLE III–B–1—PERCENT OF ADJUSTED AVERAGE DAILY OPEN INTEREST EXCLUDED AS NOT MEETING THE DEFINITION OF REFERENCED CONTRACT

| Core referenced futures contract | Year 1 percent of excluded adjusted open interest (%) | Year 2 percent of excluded adjusted open interest (%) |
|---|---|---|
| Cotton No. 2 (CT) | 0.22 | 0.00 |
| Sugar No. 11 (SB) | 0.05 | 0.00 |
| Gold (GC) | 42.59 | 0.00 |
| Silver (SI) | 48.10 | 0.00 |
| Platinum (PL) | 9.12 | 5.36 |
| Palladium (PA) | 56.87 | 6.87 |
| Copper (HG) | 37.58 | 0.25 |
| Natural Gas (NG) | 12.49 | 12.52 |
| Light Sweet Crude (CL) | 3.60 | 0.83 |
| New York Harbor ULSD (HO) | 0.96 | 1.74 |
| RBOB Gasoline (RB) | 1.34 | 1.30 |

Second, Commission staff checked and edited the remaining data to mitigate certain types of errors. Commission staff identified three general types of reporting errors and made edits to adjust the data for:

(i) Positions that were clearly reported in units of a commodity when they should have been reported in the number of gross futures-equivalent contracts. For example, a position in gold (GC) with a futures contract unit of trading of 100 ounces might be reported as 480,000 contracts, when other available information, reasonable assumptions, consultation with reporting entities and/or Commission expertise indicate that the position should have been reported as 4,800 contracts (that is, 480,000 ounces divided by 100 ounces per contract). Commission staff corrected such reported swaps position data and included the corrected data in the data set.

(ii) Positions that are not obviously reported in units of a commodity but appear to be off by one or more decimal places (*e.g.,* a position is overstated, but not by a multiple of the contract's unit of trading). For example, a position in COMEX gold is reported as 100,000 and the notional value might be reported as $13,000,000, when the price of gold is $1300 and the COMEX gold contract is for 100 ounces, indicating that the position should have been reported as 100 futures-equivalent contracts. Staff corrected such reported swaps position data and included the corrected data in the data set.

(iii) Positions reported multiple times per day or otherwise extremely different from surrounding days' reported open interest. In some cases, reporting entities submitted the same report using different reporting identifiers, for the same day. In other cases, a position would inexplicably spike for one day, to a multiple of other days' reported open interest. When Commission staff checked with the reporting entity, the reporting entity confirmed that the reports were, indeed, erroneous. Commission staff did not include such incorrectly reported duplicative swaps position data in its analysis. In other cases, positions that were clearly reported incorrectly, but for which Commission staff could discern neither a reason nor a reasonable adjustment, were not included. For example, Commission staff deleted all swap position data reports submitted by one swap dealer from its analysis because the reports were inexplicably anomalous in light of other available information, reasonable assumptions and Commission expertise. As another example, one reporting entity reported extremely large values for only certain types of positions. After speaking with the reporting entity, Commission staff determined that there was no systematic adjustment to be made, but that the actual positions were, in fact, small. Hence, Commission staff did not include such reported swaps position data in its analysis.

The number of principal records edited, resulting from the edits relating to the three types of edits to erroneous position reports noted above, is set forth in Table 2 below. A principal record is a report of a swaps open position where the reporting entity is a principal to the swap, as opposed to a counterparty record.

TABLE III–B–2—PERCENTAGE OF PRINCIPAL RECORDS ADJUSTED BY EDIT TYPE AND UNDERLYING COMMODITY, REFERENCED CONTRACTS ONLY

| | Edit type | Number of records adjusted year 1 (%) | Number of records adjusted year 2 (%) |
|---|---|---|---|
| Corn (C) | (i) | 0.00 | 0.0001 |
| | (iii) | 0.00 | 0.66 |
| Oats (O) | (iii) | 0.00 | 0.20 |
| Rough Rice (RR) | (iii) | 0.38 | 0.00 |

TABLE III–B–2—PERCENTAGE OF PRINCIPAL RECORDS ADJUSTED BY EDIT TYPE AND UNDERLYING COMMODITY, REFERENCED CONTRACTS ONLY—Continued

| | Edit type | Number of records adjusted year 1 (%) | Number of records adjusted year 2 (%) |
|---|---|---|---|
| Soybeans (S) | (i) | 0.00 | 0.03 |
| | (iii) | 2.38 | 1.46 |
| Soybean Meal (SM) | (iii) | 0.00 | 0.41 |
| Soybean Oil (SO) | (iii) | 9.15 | 4.93 |
| Wheat (W) | (i) | 0.00 | 0.01 |
| | (iii) | 1.77 | 0.71 |
| Wheat (MWE) | (iii) | 0.043 | 0.002 |
| Wheat (KW) | (iii) | 1.34 | 0.68 |
| Cocoa (CC) | (i) | 0.001 | 0.0005 |
| | (iii) | 1.79 | 0.25 |
| Coffee C (KC) | (i) | 0.00 | 0.01 |
| | (iii) | 5.33 | 0.60 |
| Cotton No. 2 (CT) | (iii) | 16.76 | 5.59 |
| FCOJ–A (OJ) | (iii) | 13.30 | 17.43 |
| Sugar No. 11 (SB) | (i) | 0.00 | 0.0009 |
| | (iii) | 1.21 | 0.54 |
| Live Cattle (LC) | (i) | 0.002 | 0.00 |
| | (iii) | 45.65 | 15.50 |
| Gold (GC) | (i) | 1.99 | 0.02 |
| | (ii) | 0.32 | 0.00 |
| | (iii) | 91.45 | 89.04 |
| Silver (SI) | (i) | 3.01 | 0.19 |
| | (iii) | 93.08 | 89.52 |
| Platinum (PL) | (i) | 2.75 | 0.01 |
| | (ii) | 0.33 | 0.01 |
| | (iii) | 23.51 | 21.11 |
| Palladium (PA) | (i) | 0.62 | 0.00 |
| | (ii) | 0.30 | 0.00 |
| | (iii) | 32.97 | 22.29 |
| Copper (HG) | (i) | 4.94 | 0.48 |
| | (iii) | 20.80 | 16.82 |
| Natural Gas (NG) | (i) | 0.01 | 1.03 |
| | (iii) | 7.68 | 3.80 |
| Light Sweet Crude (CL) | (i) | 0.001 | 0.003 |
| | (iii) | 9.53 | 8.43 |
| New York Harbor ULSD (HO) | (i) | 0.01 | 0.0006 |
| | (iii) | 29.58 | 4.33 |
| RBOB Gasoline (RB) | (i) | 0.22 | 0.60 |
| | (iii) | 30.46 | 24.62 |

Some records also appeared to contain errors attributable to other factors that Commission staff could detect and for which Commission staff can correct. For example, there were instances where the reporting entity misreported the ownership of the position, *i.e.,* principal vs. counterparty. Commission staff corrected the misreported ownership data and included the corrected data in the data set. Such corrections are important to ensure that data is not double counted. In Year 1, eight reporting entities required an adjustment to the reported position ownership information. In Year 2, five reporting entities required an adjustment to the reported position ownership information.

Third, in the part 20 large trader swap data, staff checked and adjusted the average daily open interest for positions resulting from inter-affiliate transactions and duplicative reporting of positions due to transactions between reporting entities. For an example of duplicative reporting by reporting entities (which is reporting in terms of futures-equivalent contracts), assume Swap Dealer A and Swap Dealer B have an open swap equivalent to 50 futures contracts, Swap Dealer A also has a swap equivalent to 25 futures contracts with End User X, and Swap Dealer B has a swap equivalent to 200 futures contracts with End User Y. The total open swaps in this scenario is equivalent to 275 futures contracts. However, Swap Dealer A will report a gross position of 75 contracts and Swap Dealer B will report a gross position of 250 contracts. Simply summing these two gross positions would overestimate the open swaps as 325 contracts—50 contracts more than there actually should be. For this reason, Commission staff used the counterparty accounts of each reporting entity to flag counterparty accounts of other reporting entities. Commission staff then used the daily average of the gross positions for these accounts to reduce the amount of average daily open swaps. Similarly, Commission staff flagged the counterparty accounts for entities that are affiliates of each reporting entity in order to adjust the amount of average daily open swaps. These adjustments to the Year 1 data are reflected in Table 3 below, and the corresponding adjustments to the Year 2 data are reflected in Table 4 below.

TABLE III–B–3—AVERAGE DAILY OPEN INTEREST IN YEAR 1 ADJUSTED FOR DUPLICATE AND AFFILIATE REPORTING BY UNDERLYING COMMODITY

| Paired swaps for | Average adjusted daily open interest | Average adjusted daily open interest reporting entity duplication removed | Average adjusted daily open interest reporting entity duplication & affiliates removed |
|---|---|---|---|
| Corn (C) | 655,492 | 522,566 | 359,715 |
| Oats (O) | 684 | 667 | 646 |
| Rough Rice (RR) | 916 | 640 | 362 |
| Soybeans (S) | 157,017 | 139,608 | 109,858 |
| Soybean Meal (SM) | 125,444 | 99,795 | 71,887 |
| Soybean Oil (SO) | 74,831 | 64,854 | 55,265 |
| Wheat (W) | 272,839 | 229,453 | 162,999 |
| Wheat (MGE) | 3,430 | 3,021 | 1,944 |
| Wheat (KW) | 14,918 | 14,213 | 9,436 |
| Cocoa (CC) | 15,207 | 13,792 | 11,257 |
| Coffee C (KC) | 31,540 | 28,539 | 24,164 |
| Cotton No. 2 (CT) | 51,442 | 42,806 | 35,102 |
| FCOG–A (OJ) | 160 | 142 | 121 |
| Sugar No. 11 (SB) | 279,355 | 256,887 | 211,994 |
| Live Cattle (LC) | 46,361 | 36,999 | 23,626 |
| Gold (GC) | 79,778 | 64,363 | 47,727 |
| Silver (SI) | 19,373 | 14,678 | 9,867 |
| Platinum (PL) | 25,145 | 24,530 | 21,566 |
| Palladium (PA) | 2,044 | 1,939 | 1,929 |
| Copper (HG) | 31,143 | 28,718 | 22,859 |
| Natural Gas (NG) | 4,100,419 | 3,603,368 | 2,866,128 |
| Light Sweet Crude (CL) | 2,039,963 | 1,875,660 | 1,587,450 |
| NY Harbor ULSD (HO) | 178,978 | 161,617 | 138,360 |
| RBOB Gasoline (RB) | 103,586 | 100,021 | 81,822 |

TABLE III–B–4—AVERAGE DAILY OPEN INTEREST IN YEAR 2 ADJUSTED FOR DUPLICATE AND AFFILIATE REPORTING BY UNDERLYING COMMODITY

| Paired swaps for | Average adjusted daily open interest | Average adjusted daily open interest reporting entity duplication removed | Average adjusted daily open interest reporting entity duplication & affiliates removed |
|---|---|---|---|
| Corn (C) | 1,265,639 | 960,088 | 641,014 |
| Oats (O) | 1,029 | 858 | 480 |
| Rough Rice (RR) | 396 | 250 | 4 |
| Soybeans (S) | 453,419 | 351,279 | 235,679 |
| Soybean Meal (SM) | 282,123 | 209,023 | 134,399 |
| Soybean Oil (SO) | 282,207 | 198,744 | 125,106 |
| Wheat (W) | 437,711 | 334,136 | 222,420 |
| Wheat (MWE) | 15,167 | 9,511 | 3,079 |
| Wheat (KW) | 65,533 | 47,722 | 29,563 |
| Cocoa (CC) | 141,526 | 100,564 | 56,853 |
| Coffee C (KC) | 97,128 | 74,739 | 51,846 |
| Cotton No. 2 (CT) | 137,295 | 99,496 | 60,477 |
| FCOJ–A (OJ) | 1,137 | 640 | 5 |
| Sugar No. 11 (SB) | 717,967 | 558,423 | 382,816 |
| Live Cattle (LC) | 102,131 | 77,783 | 52,330 |
| Gold (GC) | 62,804 | 50,054 | 36,029 |
| Silver (SI) | 9,306 | 6,207 | 3,510 |
| Platinum (PL) | 2,575 | 2,507 | 2,285 |
| Palladium (PA) | 889 | 857 | 823 |
| Copper (HG) | 82,479 | 65,187 | 47,365 |
| Natural Gas (NG) | 4,239,581 | 3,828,739 | 3,331,141 |
| Light Sweet Crude (CL) | 2,318,074 | 2,050,270 | 1,744,137 |
| NY Harbor ULSD (HO) | 170,316 | 117,004 | 65,721 |
| RBOB Gasoline (RB) | 102,094 | 66,560 | 30,477 |

Staff made numerous significant adjustments to the part 20 data for natural gas, due to numerous reports in units rather than the number of gross futures-equivalent contracts and the large number of reports of swaps that did not meet the definition of referenced contract.

The Commission continues to be concerned about the quality of data submitted in large trader reports pursuant to part 20 of the Commission's regulations. Commissioners and staff have expressed concerns about data reporting publicly on a variety of occasions.[515] Nevertheless, the Commission anticipates that over time part 20 submissions will become more reliable and intensive efforts by Commission staff to process and edit raw data will become less necessary. As stated in the December 2013 Position Limits Proposal, for setting subsequent levels of non-spot month limits, the Commission proposes to estimate average open interest in referenced contracts using data reported pursuant to parts 16, 20, and/or 45.[516] It is crucial, therefore, that market participants make sure they submit accurate data to the Commission, and resubmit data discovered to be erroneous, because subsequent limit levels will be based on that data. Reporting is at the heart of the Commission's market and financial surveillance programs, which are critical to the Commission's mission to protect market participants and promote market integrity. Failure to meet reporting obligations to the Commission by submitting reports and data that contain errors and omissions in violation of the part 20 regulations may subject reporting entities to enforcement actions and remedial sanctions.[517]

4. Setting Levels of Spot-Month Limits

In the December 2013 Position Limits Proposal, the Commission proposed to set the initial spot month speculative position limit levels for referenced contracts at the existing DCM-set levels for the core referenced futures contracts.[518] As an alternative, the Commission stated that it was considering using 25 percent of an exchange's estimate of deliverable supply if the Commission verified the estimate as reasonable.[519] As a further alternative, the Commission stated that it was considering setting initial spot month position limit levels at a recommended level, if any, submitted by a DCM (if lower than 25 percent of estimated deliverable supply).[520]

In determining the levels at which to repropose the initial speculative position limits, the Commission considered, without limitation, the recommendations of the exchanges as well as data to which the exchanges do not have access. In considering these and other factors, the Commission became very concerned about the effect of alternative limit levels on traders in the cash-settled referenced contracts. A DCM has reasonable discretion in establishing the manner in which it complies with core principle 5 regarding position limits.[521] As the Commission observed in the December 2013 Position Limits Proposal, ''there may be a range of spot month limits, including limits set below 25 percent of deliverable supply, which may serve as practicable to maximize . . . [the] policy objectives [set forth in section 4a(a)(3)(B) of the CEA].'' [522] The Commission must also consider the competitiveness of futures markets.[523] Thus, the Commission accepts the recommendations of the exchanges and has determined to repropose federal limits below 25 percent of deliverable supply, where setting a limit level at less than 25 percent of deliverable supply does not appear to restrict unduly positions in the cash-settled referenced contracts. The exchanges retain the ability to adopt lower exchange-set limit levels than the initial

[515] *See, e.g.,* CFTC Staff Advisory No. 15–66, available at *http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/15-66.pdf* (reminding swap dealers and major swap participants of their swap data reporting obligations); Remarks of Chairman Timothy Massad before the ABA Derivatives and Futures Law Committee, 2016 Winter Meeting, Jan. 22, 2016, available at *http://www.cftc.gov/PressRoom/SpeechesTestimony/opamassad-37* (improving data reporting).

[516] December 2013 Position Limits Proposal, 78 FR at 75734.

[517] The CFTC announced its first case enforcing the Reporting Rules in September 2015. *See* Order: Australia and New Zealand Banking Group Ltd. (''ANZ''), available at *http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfaustraliaorder091715.pdf* (the Order finds that during the period from at least March 1, 2013 through November 30, 2014, ANZ filed large trader reports that routinely contained errors).

[518] December 2013 Position Limits Proposal, 78 FR at 75727. One commenter urged the Commission to retain the legacy speculative limits for enumerated agricultural products. The ''enumerated'' agricultural products refer to the list of commodities contained in the definition of ''commodity'' in CEA section 1a; 7 U.S.C. 1a. This list of agricultural contracts includes nine currently traded contracts: Corn (and Mini-Corn), Oats, Soybeans (and Mini-Soybeans), Wheat (and Mini-wheat), Soybean Oil, Soybean Meal, Hard Red Spring Wheat, Hard Winter Wheat, and Cotton No. 2. *See* 17 CFR 150.2. The position limits on these agricultural contracts are referred to as ''legacy'' limits because these contracts on agricultural commodities have been subject to federal positions limits for decades. This commenter stated, ''There is no appreciable support within our industry or, as far as we know, from the relevant exchanges to move beyond current levels . . . . Changing current limits, as proposed in the rule, will have a negative impact on futures-cash market convergence and will compromise contract performance.'' CL–AFBF–59730 at 3. *Contra* CL–ISDA/SIFMA–59611 at 32 (setting initial spot-month limits at the existing exchange-set levels would be arbitrary because the exchange-set levels have not been calibrated to apply as ''a ceiling on the spot-month positions that a trader can hold across *all* exchanges for futures, options and swaps''); CL–ICE–59966 at 6 (''the Proposed Rule . . . effectively halves the present position limit in the spot month by aggregating across trading venues and uncleared OTC swaps''). *See also* CL–ISDA/SIFMA–59611 at 3 (the spot month limit methodology is ''both arbitrary and unjustified'').

[519] December 2013 Position Limits Proposal, 78 FR at 75727. The Commission also stated that if the Commission could not verify an exchange's estimate of deliverable supply for any commodity as reasonable, the Commission might adopt the existing DCM-set level or a higher level based on the Commission's own estimate, but not greater than would result from the exchange's estimated deliverable supply for a commodity.

One commenter was unconvinced that estimated deliverable supply is ''the appropriate metric for determining spot month position limits'' and opined that the ''real test'' should be whether limits ''allow convergence of cash and futures so that futures markets can still perform their price discovery and risk management functions.'' CL–NGFA–60941 at 2. Another commenter stated, ''While 25% may be a reasonable threshold, it is based on historical practice rather than contemporary analysis, and it should only be used as a guideline, rather than formally adopted as a hard rule. Deliverable supply is subject to numerous environmental and economic factors, and is inherently not susceptible to formulaic calculation on a yearly basis.'' CL–MGEX–60301 at 1. Another commenter expressed the view that the 25 percent formula is not ''appropriately calibrated to achieve the statutory objective'' set forth in section 4a(a)(3)(B)(i) of the CEA, 7 U.S.C. 6a(a)(3)(B)(i). CL–CME–60926 at 3. Another commenter opined that because the Commission ''has not established a relationship between 'estimated deliverable supply' and spot-month potential for manipulation or excessive speculation,'' the 25 percent formula is arbitrary. CL–ISDA/SIFMA–59611 at 31.

Several commenters opined that 25 percent of deliverable supply is too high. *E.g.,* CL–AFR–59685 at 2; CL-Tri-State Coalition for Responsible Investment-59682 at 1; CL–CMOC–59720 at 3; CL–WEED–59628 (''Only a lower limit would ensure market stability and prevent market manipulation.''); CL–Public Citizen-60313 at 1 (''There is no good reason for a single firm to take 25% of a market.''); CL–IECA–59964 at 3 (25 percent of deliverable supply ''is a lot of market power in the hands of speculators''). One commenter stated that ''position limits should be set low enough to restore a commercial hedger majority in open interest in each core referenced contract,'' CL–IATP–60323 at 5 (suggesting in a later submission that position limits at 5–10 percent of estimated deliverable supply in each covered contract applied on an aggregated basis might ''enable commercial hedgers to regain for all covered contracts their pre-2000 average share of 70 percent of agricultural contracts''). CL–IATP–60394 at 2. One commenter supported expanding position limits ''to ensure rough or approximate convergence of futures and underlying cash at expiration.'' CL–Thornton–59702 at 1.

Several commenters supported setting limits based on updated estimates of deliverable supply which reflect current market conditions. *E.g.,* CL–ICE–59966 at 5; CL–FIA–59595 at 8; CL–EEI–EPSA–59602 at 9; CL–MFA–59606 at 5; CL–CMC–59634 at 14; CL-Olam-59658 at 3; CL–CCMC–59684 at 6–7.

[520] December 2013 Position Limits Proposal, 78 FR at 75728.

[521] CEA section 5(d)(1)(B), 7 U.S.C. 7(d)(1)(B).

[522] December 2013 Position Limits Proposal, 78 FR at 75729.

[523] CEA section 15(a)(2)(B), 7 U.S.C. 19(a)(2)(B).

speculative position limit levels that the Commission reproposes today.

a. CME and MGEX Agricultural Contracts

As explained above, the Commission has verified that the estimates of deliverable supply for each of the CBOT Corn (C), Oats (O), Rough Rice (RR), Soybeans (S), Soybean Meal (SM), Soybean Oil (SO), Wheat (W) core referenced futures contract, the Hard Red Winter Wheat (KW) core referenced futures contract submitted by CME, and the Hard Red Spring Wheat (MWE) core referenced futures contract submitted by MGEX are reasonable.

Nevertheless, the Commission has determined to repropose the initial speculative spot month position limit levels for C, O, RR, S, SM, SO, W and KW at the recommended levels submitted by CME,[524] all of which are lower than 25 percent of estimated deliverable supply.[525] As is evident from the table set forth below, this also means that the Commission is reproposing the initial speculative position limit levels for these eight contracts as proposed in the December 2013 Position Limits Proposal. These initial levels track the existing DCM-set levels for the core referenced futures contracts;[526] therefore, as noted in the December 2013 Position Limits Proposal, many market participants are already used to these levels.[527] The Commission continues to believe this approach is consistent with the regulatory objectives of the Dodd-Frank Act amendments to the CEA.

TABLE III–B–5—CME AGRICULTURAL CONTRACTS—SPOT MONTH LIMIT LEVELS

| Contract | Previously proposed limit level[528] | 25% of estimated deliverable supply[529] | Reproposed speculative limit level |
|---|---|---|---|
| C | 600 | 900 | 600 |
| O | 600 | 900 | 600 |
| RR | 600 | 2,300 | 600 |
| S | 600 | 1,200 | 600 |
| SM | 720 | 2,000 | 720 |
| SO | 540 | 3,400 | 540 |
| W[530] | 600 | 1,000 | 600 |
| KW | 600 | 3,000 | 600 |

The Commission has also determined to repropose the initial speculative spot month position limit level for MWE at 1,000 contracts, which is the level requested by MGEX[531] and just slightly lower than 25 percent of estimated deliverable supply.[532] This is an increase from the previously proposed level of 600 contracts and is greater than the reproposed speculative spot month position limit levels for W and KW.[533] Upon deliberation, the Commission accepts the recommendation of MGEX.[534]

TABLE III–B–6—CME AND MGEX AGRICULTURAL CONTRACTS—SPOT MONTH

| Core referenced futures contract | Basis of spot-month level | Limit level | Unique persons over spot month limit | | Reportable persons spot month only |
|---|---|---|---|---|---|
| | | | Cash settled contracts | Physical delivery contracts | |
| Corn (C) | CME recommendation | **† 600** | 0 | 36 | 1,050 |
| | 25% DS | 900 | 0 | 20 | |
| Oats (O) | CME recommendation | **† 600** | 0 | 0 | 33 |
| | 25% DS | 900 | 0 | 0 | |
| Soybeans (S) | CME recommendation | **† 600** | 0 | 22 | 929 |
| | 25% DS | 1,200 | 0 | 14 | |
| Soybean Meal (SM) | CME recommendation | **† 720** | 0 | 14 | 381 |
| | 25% DS | 2,000 | 0 | * | |

[524] CL–CME–61007 at 5.

[525] The Commission noted in the December 2013 Position Limits Proposal ''that DCMs historically have set or maintained exchange spot month limits at levels below 25 percent of deliverable supply.'' December 2013 Position Limits Proposal, 78 FR at 75729.

[526] *See* CL–CME–61007 (specifying lower exchange-set limit levels for W and RR in certain circumstances).

[527] December 2013 Position Limits Proposal, 78 FR at 75727.

[528] December 2013 Position Limits Proposal, 78 FR at 75839 (Appendix D to Part 150—Initial Position Limit Levels).

[529] Rounded up to the next 100 contracts.

[530] The W core referenced futures contract refers to soft red winter wheat, the KW core reference futures contract refers to hard red winter wheat, and the MWE core reference futures contract refers to hard red spring wheat; *i.e.,* the contracts are for different products.

[531] CL–MGEX–61038 at 2; *see also* CL–MGEX–60938 at 2 (earlier submission of deliverable supply estimate).

[532] The difference is due to rounding. The MGEX estimate of 4,005 contract equivalents for MWE deliverable would have supported a spot-month limit level of 1,100 contracts (rounded up to the next 100 contracts). The Commission noted in the December 2013 Position Limits Proposal ''that DCMs historically have set or maintained exchange spot month limits at levels below 25 percent of deliverable supply.'' December 2013 Position Limits Proposal, 78 FR at 75729.

[533] Most commenters who supported establishing the same level of speculative limits for each of the three wheat core referenced futures contracts focused on parity in the non-spot months. However, some commenters did support wheat party in the spot month. *See, e.g.,* CL–CMC–59634 at 15; CL–NCFC–59942 at 6.

[534] The difference between an estimate of 4,000 contracts, which would result in a limit level of 1,000, and 4,005 contracts, which results in a limit level of 1,100 contracts, is small enough that the Commission's prior statements regarding the 25% formula are instructive. As stated in the December 2013 Position Limits Proposal, the 25 percent formula ''is consistent with the longstanding acceptable practices for DCM core principle 5 which provides that, for physical-delivery contracts, the spot-month limit should not exceed 25 percent of the estimated deliverable supply.'' December 2013 Position Limits Proposal, 78 FR at 75729. The Commission continues to believe, based on its experience and expertise, that the 25 percent formula is an ''effective prophylactic tool to reduce the threat of corners and squeezes, and promote convergence without compromising market liquidity.'' December 2013 Position Limits Proposal, 78 FR at 75729.

TABLE III–B–6—CME AND MGEX AGRICULTURAL CONTRACTS—SPOT MONTH—Continued

| Core referenced futures contract | Basis of spot-month level | Limit level | Unique persons over spot month limit | | Reportable persons spot month only |
|---|---|---|---|---|---|
| | | | Cash settled contracts | Physical delivery contracts | |
| Soybean Oil (SO) | CME recommendation | †**540** | 0 | 21 | 397 |
| | 25% DS | 3,400 | 0 | 0 | |
| Wheat (W) | CME recommendation | †**600** | 0 | 11 | 444 |
| | 25% DS | 1,000 | 0 | 6 | |
| Wheat (MWE) | Parity w/CME recommendation | †**600** | 0 | * | 102 |
| | 25% DS | ††**1,000** | 0 | * | |
| Wheat (KW) | CME recommendation | †**600** | 0 | 4 | 250 |
| | 25% DS (MW) | 1,000 | 0 | * | |
| | 25% DS (KW) | 3,000 | 0 | * | |
| Rough Rice (RR) | CME recommendation | †**600** | 0 | 0 | 91 |
| | 25% DS | 2,300 | 0 | 0 | |

Reproposed speculative position limit levels are shown in **bold**.
''25% DS'' means 25 percent of the deliverable supply as estimated by the exchange listing the core referenced futures contract.
† Denotes existing limit level.
†† Limit level requested by MGEX.
* Denotes fewer than 4 persons.

The Commission's impact analysis reveals no traders in cash settled contracts in any of C, O, S, SM, SO, W, MWE, KW, or RR, and no traders in physical delivery contracts for O and RR, above the initial speculative limit levels for those contracts. The Commission found varying numbers of traders in the C, S, SM, SO, W, MWE, KW physical delivery contracts over the initial levels, but the numbers were very small for MWE and KW.[535] Because the levels that the Commission reproposes today for C, O, S, SM, SO, W, KW, and RR maintain the status quo for those contracts, the Commission assumes that some or possibly all of such traders over the initial levels are hedgers. Hedgers may have to file for an applicable exemption, but hedgers with bona fide hedging positions should not have to reduce their positions as a result of speculative position limits per se. Thus, the number of traders in the C, S, SM, SO, W and KW physical delivery contracts who would need to reduce speculative positions below the initial limit levels should be lower than the numbers indicated by the impact analysis. The Commission believes that setting initial speculative levels at 25 percent of deliverable supply would, based upon logic and the Commission's impact analysis, affect fewer traders in the C, S, SM, SO, W and KW physical delivery contracts. Consistent with its statement in the December 2013 Position Limits Proposal, the Commission believes that accepting the recommendation of the DCM to set these lower levels of initial spot month limits will serve the objectives of preventing excessive speculation, manipulation, squeezes and corners,[536] while ensuring sufficient market liquidity for bona fide hedgers in the view of the listing DCM and ensuring that the price discovery function of the market is not disrupted.[537]

b. Softs

As explained above, the Commission has verified that the estimates of deliverable supply for each of the IFUS Cocoa (CC), Coffee ''C'' (KC), Cotton No. 2 (CT), FCOJ–A (OJ), Sugar No. 11 (SB), and Sugar No. 16 (SF) core referenced futures contracts submitted by ICE are reasonable.

The Commission has determined to repropose the initial speculative spot month position limit levels for the CC, KC, CT, OJ, SB, and SF[538] core referenced futures contracts at 25 percent of estimated deliverable supply, based on the estimates of deliverable supply submitted by ICE.[539] As is evident from the table set forth below, this also means that the Commission is reproposing initial speculative position limit levels that are significantly higher than the levels for these six contracts as previously proposed. As stated in the December 2013 Position Limits Proposal, the 25 percent formula ''is consistent with the longstanding acceptable practices for DCM core principle 5 which provides that, for physical-delivery contracts, the spot-month limit should not exceed 25 percent of the estimated deliverable supply.''[540] The Commission continues to believe, based on its experience and expertise, that the 25 percent formula is an ''effective prophylactic tool to reduce the threat of corners and squeezes, and promote convergence without compromising market liquidity.''[541]

TABLE III–B–7—IFUS SOFT AGRICULTURAL CONTRACTS—SPOT MONTH LIMIT LEVELS

| Contract | Previously proposed limit level[542] | 25% of estimated deliverable supply[543] | Reproposed speculative limit level |
|---|---|---|---|
| CC | 1,000 | 5,500 | 5,500 |

[535] Four or fewer traders.

[536] *Contra* CL–ISDA/SIFMA–59611 at 55 (proposed spot month limits ''are almost certainly far smaller than necessary to prevent corners or squeezes'').

[537] December 2013 Position Limits Proposal, 78 FR at 75729.

[538] One commenter supported considering ''tropicals (sugar/coffee/cocoa) . . . separately from those agricultural crops produced in the US domestic market.'' CL–Thornton–59702 at 1; *see also* CL–Armajaro–59729 at 1.

[539] CL–IFUS–60807.

[540] December 2013 Position Limits Proposal, 78 FR at 75729. The Commission also noted ''that DCMs historically have set or maintained exchange spot month limits at levels below 25 percent of deliverable supply.'' December 2013 Position Limits Proposal, 78 FR at 75729.

[541] December 2013 Position Limits Proposal, 78 FR at 75729.

TABLE III–B–7—IFUS SOFT AGRICULTURAL CONTRACTS—SPOT MONTH LIMIT LEVELS—Continued

| Contract | Previously proposed limit level [542] | 25% of estimated deliverable supply [543] | Reproposed speculative limit level |
|---|---|---|---|
| KC | 500 | 2,400 | 2,400 |
| CT | 300 | 1,600 | 1,600 |
| OJ | 300 | 2,800 | 2,800 |
| SB | 5,000 | 23,300 | 23,300 |
| SF | 1,000 | 7,000 | 7,000 |

The Commission did not receive any estimate of deliverable supply for the CME Live Cattle (LC) core referenced futures contract from CME, nor did CME recommend any change in the limit level for LC. In the absence of any such update, the Commission is reproposing the initial speculative position limit level of 450 contracts. Of 616 reportable persons, the Commission's impact analysis did not reveal any unique person trading cash settled or physical delivery spot month contracts who would have held positions above this level for LC.

With respect to the IFUS CC, KC, CT, OJ, SB, and SF core referenced futures contracts, the Commission's impact analysis did not reveal any unique person trading cash settled spot month contracts who would have held positions above the initial levels that the Commission adopts today; as illustrated below, lower levels would mostly have affected small numbers of traders in physical delivery contracts.

TABLE III–B–8—IFUS SOFT AGRICULTURAL CONTRACTS—SPOT MONTH

| Core referenced futures contract | Basis of spot-month level | Limit level | Unique persons over spot month limit | | Reportable persons spot month only |
|---|---|---|---|---|---|
| | | | Cash settled contracts | Physical delivery contracts | |
| Cocoa (CC) | 15% DS | 3,300 | 0 | 0 | 164 |
| | 25% DS | ††**5,500** | 0 | 0 | |
| Coffee "C" (KC) | 15% DS | 1,440 | 0 | * | 336 |
| | 25% DS | ††**2,400** | 0 | * | |
| Cotton No. 2 (CT) | 15% DS | 960 | 0 | * | 122 |
| | 25% DS | ††**1,600** | 0 | 0 | |
| FCOJ–A (OJ) | 15% DS | 1,680 | 0 | 0 | 38 |
| | 25% DS | ††**2,800** | 0 | 0 | |
| Sugar No. 11 (SB) | 15% DS | 13,980 | * | 10 | 443 |
| | 25% DS | ††**23,300** | 0 | * | |
| Sugar No. 16 (SF) | 15% DS | 4,200 | 0 | 0 | 12 |
| | ††25% DS | ††**7,000** | 0 | 0 | |

Reproposed speculative position limit levels are shown in **bold**.
"15% DS" means 15 percent of the deliverable supply as estimated by the exchange listing the core referenced futures contract and is included to provide information regarding the distribution of reportable traders.
"25% DS" means 25 percent of the deliverable supply as estimated by the exchange listing the core referenced futures contract.
†† Limit level requested by ICE.
* Denotes fewer than 4 persons.

c. Metals

As explained above, the Commission has verified that the estimates of deliverable supply for each of the COMEX Gold (GC), COMEX Silver (SI), NYMEX Platinum (PL), NYMEX Palladium (PA), and COMEX Copper (HG) core referenced futures contracts submitted by CME are reasonable.

Nevertheless, the Commission has determined to repropose the initial speculative spot month position limit levels for GC, SI, and HG at the recommended levels submitted by CME,[544] all of which are lower than 25 percent of estimated deliverable supply.[545] In the case of GC and SI, this is a doubling of the current exchange-set limit levels.[546] In the case of HG, the initial level is the same as the existing DCM-set level for the core referenced futures contract and lower than the level previously proposed.

TABLE III–B–9—CME METALS CONTRACTS—SPOT MONTH LIMIT LEVELS

| Contract | Previously proposed limit level [547] | 25% of estimated deliverable supply [548] | Reproposed speculative limit level |
|---|---|---|---|
| GC | 3,000 | 11,200 | 6,000 |

[542] December 2013 Position Limits Proposal, 78 FR at 75839–40 (Appendix D to Part 150—Initial Position Limit Levels).

[543] Rounded up to the next 100 contracts.

[544] CL–CME–61007 at 5.

[545] The Commission noted in the December 2013 Position Limits Proposal "that DCMs historically have set or maintained exchange spot month limits at levels below 25 percent of deliverable supply." December 2013 Position Limits Proposal, 78 FR at 75729.

[546] One commenter cautioned against raising limit levels for GC to 25 percent of deliverable supply, and expressed concern that higher federal limits would incentivize exchanges to raise their own limits. CL–WGC–59558 at 2–4.

TABLE III–B–9—CME METALS CONTRACTS—SPOT MONTH LIMIT LEVELS—Continued

| Contract | Previously proposed limit level [547] | 25% of estimated deliverable supply [548] | Reproposed speculative limit level |
|---|---|---|---|
| SI | 1,500 | 5,600 | 3,000 |
| PL | 500 | 900 | 100 |
| PA | 650 | 900 | −500 |
| HG | 1,200 | 1,100 | 1,000 |

The Commission has also determined to repropose the initial speculative spot month position limit level for PL at 100 contracts and PA at 500 contracts, which are the levels recommended by CME. In the case of PL and PA, the reproposed level is the same as the existing DCM-set level for the core referenced futures contract, and a decrease from the previously proposed levels of 500 and 650 contracts, respectively.

The Commission found varying numbers of traders in the GC, SI, PL, PA, and HG physical delivery contracts over the initial levels, but the numbers were very small except for PA.[549] Because the levels that the Commission reproposes today for PL, PA, and HG maintain the status quo for those contracts, the Commission assumes that some or possibly all of such traders over the reproposed levels are hedgers. The Commission reiterates the discussion above regarding agricultural contracts: hedgers may have to file for an applicable exemption, but hedgers with bona fide hedging positions should not have to reduce their positions as a result of speculative position limits per se. Thus, the number of traders in the metals physical delivery contracts who would need to reduce speculative positions below the reproposed limit levels should be lower than the numbers indicated by the impact analysis. And, while setting initial speculative levels at 25 percent of deliverable supply would, based upon logic and the Commission's impact analysis, affect fewer traders in the metals physical delivery contracts, consistent with its statement in the December 2013 Position Limits Proposal, the Commission believes that setting these lower levels of initial spot month limits will serve the objectives of preventing excessive speculation, manipulation, squeezes and corners,[550] while ensuring sufficient market liquidity for bona fide hedgers in the view of the listing DCM and ensuring that the price discovery function of the market is not disrupted.

TABLE III–B–10—CME METAL CONTRACTS—SPOT MONTH

| Core referenced futures contract | Basis of spot-month level | Limit level | Unique persons over spot month limit: Cash settled contracts | Unique persons over spot month limit: Physical delivery contracts | Reportable persons spot month only |
|---|---|---|---|---|---|
| Gold (GC) | CME recommendation | **6,000** | * | * | 518 |
| | 25% DS | 11,200 | 0 | 0 | |
| Silver (SI) | CME recommendation | **3,000** | 0 | 0 | 311 |
| | 25% DS | 5,600 | 0 | 0 | |
| Platinum (PL) | CME recommendation | † **500** | 13 | * | 235 |
| | 25% DS | 900 | 10 | * | |
| | 50% DS | 1,800 | * | 0 | |
| Palladium (PA) | CME recommendation | † **100** | 6 | 14 | 164 |
| | 25% DS | 900 | 0 | 0 | |
| Copper (HG) | CME recommendation | † **1,000** | 0 | * | 493 |
| | 25% DS | 1,100 | 0 | * | |

Reproposed speculative position limit levels are shown in **bold**.
"25% DS" means 25 percent of the deliverable supply as estimated by the exchange listing the core referenced futures contract.
"50% DS" means 50 percent of the deliverable supply as estimated by the exchange listing the core referenced futures contract and is included to provide information regarding the distribution of reportable traders.
† Denotes existing exchange-set limit level.
* Denotes fewer than 4 persons.

The Commission's impact analysis reveals no unique persons in the SI and HG cash settled referenced contracts, and very few unique persons in the cash settled GC referenced contract, whose positions would have exceeded the initial limit levels for those contracts. Based on the Commission's impact analysis, setting the initial federal spot month limit levels for PL and PA at the lower levels recommended by CME would impact a few traders in PL and PA cash settled contracts.

The Commission has carefully considered the numbers of unique persons that would be impacted by each of the cash-settled and physical-delivery spot month limits in the PL and PA referenced contracts. The Commission notes those limits would appear to impact more traders in the physical-delivery PA contract than in the cash-settled PA contract, while fewer traders would be impacted in the physical-delivery PL contract than in the cash-settled PL contract (in any event, few traders would appear to be affected).[551]

[547] December 2013 Position Limits Proposal, 78 FR at 75840 (Appendix D to Part 150—Initial Position Limit Levels).

[548] Rounded up to the next 100 contracts.

[549] Fewer than four unique persons.

[550] *Contra* CL–ISDA/SIFMA–59611 at 55 (proposed spot month limits "are almost certainly far smaller than necessary to prevent corners or squeezes").

[551] In this regard, the Commission notes that CME did not have access to the Commission's impact analysis when CME recommended levels for its physical-delivery core referenced futures contracts.

The Commission also observed the distribution of those cash-settled traders over time; as reflected in the open interest table discussed below regarding setting non-spot month limits, it can be readily observed that open interest in each of the cash-settled PL and PA referenced contracts was markedly lower in the second 12-month period (year 2) than in the prior 12-month period (year 1). Accordingly, the Commission accepts the CME recommended levels in PL and PA referenced contracts.

d. Energy

As explained above, the Commission has verified that the estimates of deliverable supply for each of the NYMEX Natural Gas (NG), Light Sweet Crude (CL), NY Harbor ULSD (HO), and RBOB Gasoline (RB) core referenced futures contracts submitted by CME are reasonable.

The Commission has determined to repropose the initial speculative spot month position limit levels for the NG, CL, HO, and RB core referenced futures contracts at 25 percent of estimated deliverable supply which, in the case of CL, HO, and RB is higher than the levels recommended by CME.[552] As is evident from the table set forth below, this also means that the Commission is reproposing speculative position limit levels that are significantly higher than the levels for these four contracts as previously proposed. As stated in the December 2013 Position Limits Proposal, the 25 percent formula ''is consistent with the longstanding acceptable practices for DCM core principle 5 which provides that, for physical-delivery contracts, the spot-month limit should not exceed 25 percent of the estimated deliverable supply.'' [553] The Commission continues to believe, based on its experience and expertise, that the 25 percent formula is an ''effective prophylactic tool to reduce the threat of corners and squeezes, and promote convergence without compromising market liquidity.'' [554]

TABLE III–B–11—CME ENERGY CONTRACTS—SPOT MONTH LIMIT LEVELS

| Contract | Previously proposed limit level [555] | 25% of estimated deliverable supply [556] | Reproposed speculative limit level |
|---|---|---|---|
| NG | 1,000 | 2,000 | 2,000 |
| CL | 3,000 | 10,400 | 10,400 |
| HO | 1,000 | 2,900 | 2,900 |
| RB | 1,000 | 6,800 | 6,800 |

The levels that CME recommended for NG, CL, HO, and RB are twice the existing exchange-set spot month limit levels. Nevertheless, the Commission is reproposing speculative spot month limit levels at 25 percent of deliverable supply for CL, HO, and RB because the Commission believes that higher levels will lessen the impact on a number of traders in both cash settled and physical delivery contracts. For NG, the Commission is reproposing the physical delivery limit at 25% of deliverable supply, as recommended by CME; [557] the Commission is also reproposing a conditional spot month limit exemption of 10,000 for cash-settled contracts in natural gas only.[558] This exemption would to some degree maintain the status quo in natural gas because each of the NYMEX and ICE cash-settled natural gas contracts, which settle to the final settlement price of the physical delivery contract, include a conditional spot month limit exemption of 5,000 contracts (for a total of 10,000 contracts).[559] However, neither the

[552] CL–CME–61007 at 5. One commenter opined that 25 percent of deliverable supply would result in a limit level that is too high for natural gas, and suggest 5 percent as an alternative that ''would provide ample liquidity and significantly reduce the potential for excessive speculation.'' CL–Industrial Energy Consumers of America–59964 at 3. Another commenter supported increasing ''the spot-month position limit levels for Henry Hub Natural Gas referenced contracts to be consistent with CME Group's or ICE's estimates of deliverable supply and more generally the significant new sources of natural gas.'' CL–NGSA–59674 at 3.

[553] December 2013 Position Limits Proposal, 78 FR at 75729.

[554] December 2013 Position Limits Proposal, 78 FR at 75729.

[555] December 2013 Position Limits Proposal, 78 FR at 75840 (App. D to part 150—Initial Position Limit Levels).

[556] Rounded up to the next 100 contracts.

[557] One commenter expressed concern about setting the spot month limit for natural gas swaps at the same level as for the physically settled futures contract, because some referenced contracts cease to be economically equivalent ''during the limited window at expiry.'' CL–BG Group–59937 at 3.

[558] This exemption for up to 10,000 contracts would be five times the spot month limit of 2,000 contracts, consistent with the December 2013 Position Limits Proposal. *See* December 2013 Position Limits Proposal, 78 FR at 75736–8. Under vacated § 151.4, the Commission would have applied a spot-month position limit for cash-settled contracts in natural gas at a level of five times the level of the limit for the physical delivery core referenced futures contract. *See* Position Limits for Futures and Swaps, 76 FR 71626, 71687 (Nov. 18, 2011).

[559] Some commenters supported retaining a conditional spot month limit in natural gas. *E.g.*, CL–ICE–60929 at 12 (''Any changes to the current terms of the Conditional Limit would disrupt present market practice for no apparent reason. Furthermore, changing the limits for cash-settled contracts would be a significant departure from current rules, which have wide support from the broader market as evidenced by multiple public comments supporting no or higher cash-settled limits.''). *Contra* CL-Sen. Levin–59637 at 7 (''The proposed higher limit for cash settled contracts is ill-advised. It would not only raise the affected position limits to levels where they would be effectively meaningless, it would also introduce market distortions favoring certain contracts and certain exchanges over others, and potentially disrupt important markets, including the U.S. natural gas market that is key to U.S. manufacturing.''); CL-Public Citizen–59648 at 5 (''Congress, in allowing an exemption for bona fide hedgers but not pure speculators, could not possibly have intended for the Commission to implement position limits that allow market speculators to hold 125 percent of the estimated deliverable supply. Once again, while this exception for cash-settled contracts would avoid market manipulations such as corners and squeezes (since cash-settled contracts give no direct control over a commodity), it does not address the problem of undue speculative influence on futures prices.''); CL-Better Markets-60401 at 17 (''There is no justification for treating cash and physically-settled contracts differently in any month, and settlement characteristics should not be a determinant of the ability to exceed the limits in any month.''). One commenter urged the Commission ''to eliminate the requirement that traders hold no physical-delivery position in order to qualify for the conditional spot-month limit exemption'' in order to maintain liquidity in the NYMEX natural gas futures contract. CL–BG Group–59656 at 6–7. *See also* CL–NGSA–59674 at 38–39 (supporting the higher conditional spot month limit in natural gas without restricting positions in the underlying physical delivery contract); CL–EEI–EPSA–59602 at 10 (the Commission should permit ''market participants to rely on higher speculative limits for cash-settled contracts while still holding a position in the physical-delivery contract''); CL–APGA–59722 at 8 (the Commission should condition the spot month limit exemption for cash settled natural gas contracts by precluding a trader from holding more than one quarter of the deliverable supply in physical inventory). *Cf.* CL–CME–59971 at 3 (eliminate the five times natural gas limit because it ''encourages participants to depart from, or refrain from establishing positions in, the primary physical delivery contract market and instead opt for the cash-settled derivative contract market, especially during the last three trading days when the five times limit applies. By encouraging departure from the primary contract market, the five

NYMEX and ICE penultimate contracts, which settle to the daily settlement price on the next to last trading day of the physical delivery contract, nor OTC swaps, are currently subject to any spot month position limit. In addition, the Commission's impact analysis suggests that a conditional spot month limit exemption greater than 25% of deliverable supply for cash settled contracts in natural gas would potentially benefit many traders.

TABLE III–B–12—ENERGY CONTRACTS—SPOT MONTH

| Core referenced futures contract | Basis of spot-month level | Limit level | Unique persons over spot month limit: Cash settled contracts | Unique persons over spot month limit: Physical delivery contracts | Reportable persons spot month only |
|---|---|---|---|---|---|
| Natural Gas (NG) | CME recommendation | **2,000** | 131 | 16 | 1,400 |
| | 50% DS | 4,000 | 77 | * | |
| | Conditional Exemption | 10,000 | 20 | 0 | |
| Light Sweet Crude (CL) | CME recommendation | †† 6,000 | 19 | 8 | 1,733 |
| | 25% DS | **10,400** | 16 | * | |
| | 50% DS | 20,800 | * | 0 | |
| NY Harbor ULSD (HO) | CME recommendation | 2,000 | 24 | 11 | 470 |
| | 25% DS | **2,900** | 15 | 5 | |
| | 50% DS | 5,800 | 5 | 0 | |
| RBOB Gasoline (RB) | CME recommendation | 2,000 | 23 | 14 | 463 |
| | 25% DS | **6,800** | * | 0 | |
| | 50% DS | 13,600 | 0 | 0 | |

Reproposed speculative position limit levels are shown in **bold**.
"25% DS" means 25 percent of the deliverable supply as estimated by the exchange listing the core referenced futures contract.
"50% DS" means 50 percent of the deliverable supply as estimated by the exchange listing the core referenced futures contract and is included to provide information regarding the distribution of reportable traders.
†† CME recommended a step-down spot month limit of 6,000/5,000/4,000 contracts in the last three days of trading.
* Denotes fewer than 4 persons.

### 5. Setting Levels of Single-Month and All-Months-Combined Limits

The Commission has determined to use the futures position limits formula, 10 percent of the open interest for the first 25,000 contracts and 2.5 percent of the open interest thereafter, to repropose the non-spot month speculative position limits for referenced contracts, subject to the details and qualifications set forth in this Notice.[560] The Commission continues to believe that ''the non-spot month position limits would restrict the market power of a speculator that could otherwise be used to cause unwarranted price movements.'' [561]

#### a. CME and MGEX Agricultural Contracts

The Commission is reproposing the non-spot month speculative position limit levels for the Corn (C), Oats (O), Rough Rice (RR), Soybeans (S), Soybean Meal (SM), Soybean Oil (SO), and Wheat (W) core referenced futures contracts based on the 10, 2.5 percent open interest formula.[562] Based on the Commission's experience since 2011 with non-spot month speculative position limit levels for the Hard Red Winter Wheat (KW) and Hard Red Spring Wheat (MWE) core referenced futures contracts, the Commission is reproposing the limit levels for those two commodities at the current level of 12,000 contracts rather than reducing them to the lower levels that would result from applying the 10, 2.5 percent formula.[563]

times limit encourages a process of de-liquefying the benchmark physically delivered futures market and directly affects the determination of the final settlement price for the NYMEX NG contract- the very same price that a position representing five times the physical limit will settle against.'').

[560] As noted in the December 2013 Position Limits Proposal, the Commission has used the 10, 2.5 percent formula in administering the level of the legacy all-months position limits since 1999. December 2013 Position Limits Proposal, 78 FR at 75729–30.

Several commenters did not support establishing non-spot month limits. *See, e.g.,* CL–ISDA/SIFMA–59611 at 27 (''There is no justification *whatsoever* for non-spot-month limits.''); CL–EEI–EPSA–59602 at 10 (''limits outside the spot month are not necessary''); CL–AMG–59709 at 10 (the Commission should ''decline to adopt non-spot-month position limits''); CL–CME–59718 at 39 (the Proposal's non-spot-month position limit formula should be withdrawn''); CL–CAM–60097 at 2 (''Non-spot month limits are neither necessary nor appropriate.''); CL–BG Group–60383 at 2 (''Any final rule should be limited to a federally mandated spot-month limit (not any/all month limits).''). Some of these same commenters supported position accountability in the non-spot months rather than limits. *See, e.g.,* CL–EEI–EPSA–59602 at 10, CL–FIA–59595 at 3, CL–MFA–60385 at 5, CL–ISDA/SIFMA–59611 at 29, CL–Calpine–59663 at 3–4, CL–Working Group-60396 at 10, CL–EDF–60398 at 4, CL–ICE–59966 at 8, CL–BG Group-60383 at 2, CL–CMC–59634 at 11. Some commenters also urged the Commission to wait until it has reliable data before establishing non-spot month limits. *See, e.g.,* CL–EEI–EPSA–59602 at 11; CL–FIA–59595 at 3, 14; CL–MFA–60385 at 5; CL–ISDA/SIFMA–59611 at 29; CL–Olam–59658 at 1, 3. *See also* discussion of part 20 data adjustments under § 150.2, below. *Contra* CL–O SEC–59972 (''corners and other supply fluctuations can occur during non-spot months'').

A commenter who did not support adopting non-spot month limits suggested a fall-back position of adopting ''any months limits'' but not ''all months limits,'' and suggested an alternative 10, 5 percent formula in specified circumstances. CL-Working Group–59693 at 62. *See also* CL–CME–59718 at 44 (supporting a 10, 5 percent formula). One commenter supported abolishing single month limits ''in favor of an ''all months'' or gross position that would effectively allow the player to adapt their position to the realities of an agricultural crop that doesn't flow in equal monthly chunks.'' CL-Thornton–59702 at 1. Another commenter stated that ''[p]osition limits should be a function of the liquidity of the market,'' CL–MFA–59606 at 21, and asserted that applying the 10, 2.5 percent formula will result in ''a self-reinforcing cycle of lower open interest and lower position limits in successive years.'' CL–MFA–59696 at 22. Another commenter supported ''tying the overall non-spot month position limits to an acceptable aggregate (market-wide) level of speculation, and tying individual trader limits to that aggregate level.'' CL-Public Citizen–59648 at 4. Another commenter expressed the belief that the 10, 2.5 percent formula would result in non-spot month limits that ''are much too high to adequately regulate excessive speculation that might lead to price fluctuations.'' CL–Tri-State–59682 at 1. To ''address the cumulative, disruptive effect of traders who hold large, but not dominant positions,'' one commenter suggested basing non-spot month position limits on ''an acceptable total level of speculation that approximates the historic ratio of hedging to investor/speculative trading.'' CL–A4A–59714 at 4. *See* CL-Better Markets–60401 at 4 (''Historically, speculators in commodity futures have constituted between 15%–30% of market activity, and within this range speculators productively facilitated effective hedging without meaningfully disrupting or independently shaping the market's behavior.'').

[561] December 2013 Position Limits Proposal, 78 FR at 75730.

[562] One commenter expressed concern ''that proposed all-months-combined speculative position limits based on open interest levels is not necessarily the appropriate methodology and could lead to contract performance problems.'' This commenter urged ''that all-months-combined limits be structured to 'telescope' smoothly down to legacy spot-month limits in order to ensure continued convergence.'' CL–NGFA–60312 at 4.

[563] One commenter supported a higher limit for KW than proposed to promote growth and to enable liquidity for Kansas City hedgers who often use the Chicago market. CL-Citadel-59717 at 8. Another

Continued

TABLE III–B–13—CME AND MGEX AGRICULTURAL CONTRACTS—NON-SPOT MONTH LIMIT LEVELS

| Contract | Current limit level | Previously proposed limit level | Reproposed speculative limit level |
|---|---|---|---|
| C | 33,000 | 53,500 | 62,400 |
| O | 2,000 | 1,600 | 5,000 |
| RR | 1,800 | 2,200 | 5,000 |
| S | 15,000 | 26,900 | 31,900 |
| SM | 6,500 | 9,000 | 16,900 |
| SO | 8,000 | 11,900 | 16,700 |
| W [564] | 12,000 | 16,200 | 32,800 |
| KW | 12,000 | 6,500 | 12,000 |
| MWE | 12,000 | 3,300 | 12,000 |

Maintaining the status quo for the non-spot month limit levels for the KW and MWE core referenced futures contracts means there will be partial wheat parity.[565] The Commission has determined not to raise the reproposed limit levels for KW and MWE to the limit level for W, as 32,800 contracts appears to be extraordinarily large in comparison to open interest in the KW and MWE markets, and the limit levels for KW and MWE are already larger than a limit level based on the 10, 2.5 percent formula. Even when relying on a single criterion, such as percentage of open interest, the Commission has historically recognized that there can ''result . . . a range of acceptable position limit levels.'' [566]

TABLE III–B–14—CME AND MGEX AGRICULTURAL CONTRACTS—NON-SPOT MONTHS

| Core-referenced futures contract | Open interest: Year | Futures | Swaps | Total | Initial limit level | Unique persons above limit level: All months | Single month | Reportable persons in market—all months |
|---|---|---|---|---|---|---|---|---|
| Corn (C) | 1 | 1,829,359 | 359,715 | 2,189,074 | **62,400** | * | * | 2,606 |
| | 2 | 1,779,977 | 641,014 | 2,420,991 | | | | |
| Oats (O) | 1 | 10,097 | 646 | 10,743 | **5,000** | 0 | 0 | 173 |
| | 2 | 11,223 | 480 | 11,703 | | | | |
| Rough Rice (RR) | 1 | 10,585 | 362 | 10,948 | **5,000** | 0 | 0 | 281 |
| | 2 | 12,769 | 4 | 12,773 | | | | |
| Soybeans (S) | 1 | 973,037 | 109,858 | 1,082,895 | **31,900** | 6 | 4 | 2,503 |
| | 2 | 962,636 | 235,679 | 1,198,315 | | | | |
| Soybean Meal (SM) | 1 | 422,611 | 71,887 | 494,498 | **16,900** | 5 | 4 | 978 |
| | 2 | 463,549 | 134,399 | 597,948 | | | | |
| Soybean Oil (SO) | 1 | 421,114 | 55,265 | 476,379 | **16,700** | 5 | 4 | 1,034 |
| | 2 | 464,373 | 125,106 | 589,478 | | | | |
| Wheat (W) | 1 | 1,072,107 | 162,999 | 1,235,105 | **32,800** | * | * | 1,867 |
| | 2 | 1,010,342 | 222,420 | 1,232,762 | | | | |
| Wheat (MWE) | 1 | 67,653 | 1,944 | 69,596 | † 5,000 | 10 | 7 | 342 |
| | 2 | 66,608 | 3,079 | 69,687 | **12,000** | 0 | 0 | |
| Wheat (KW) | 1 | 169,059 | 9,436 | 178,495 | † 8,100 | 9 | 8 | 718 |
| | 2 | 216,236 | 29,563 | 245,799 | **12,000** | * | * | |

Year 1 = July 1, 2014 to June 30, 2015
Year 2 = July 1, 2015 to June 30, 2016
Reproposed speculative position limit levels are shown in **bold**.
† Application of the 10, 2.5 percent formula would result in a level lower than the level adopted by the Commission in 2011.
* Denotes fewer than 4 persons.

## b. Softs

The Commission is reproposing non-spot month speculative position limit levels for the CC, KC, CT, OJ, SB, SF and LC [567] core referenced futures contracts based on the 10, 2.5 percent open interest formula.

commenter supported setting ''a non-spot month and combined position limit of no less than 12,000 for all three wheat contracts.'' CL–MGEX–60301 at 1. *Contra* CL–O SEC–59972 at 7–8 (commending ''the somewhat more restrictive limitations . . . on wheat trading'').

[564] The W core referenced futures contract refers to soft red winter wheat, the KW core reference futures contract refers to hard red winter wheat, and the MWE core reference futures contract refers to hard red spring wheat; *i.e.,* the contracts are for different products.

[565] Several commenters supported adopting equivalent non-spot month position limits for the three existing wheat referenced contracts traders. *See, e.g.,* CL–FIA–59595 at 4, 15; CL–CMC–60391 at 8; CL–CMC–60950 at 11; CL–CME–59718 at 44; CL–AFBF–59730 at 4; CL–MGEX–59932 at 2; CL–MGEX–60301 at 1; CL–MGEX–59610 at 2–3; CL–MGEX–60936 at 2–3; CL–NCFC–59942 at 6; CL–NGFA–59956 at 3.

[566] Revision of Speculative Position Limits, 57 FR 12770, 12766 (Apr. 13, 1992). *See also* Revision of Speculative Position Limits and Associated Rules, 63 FR 38525, 38527 (July 17, 1998). *Cf.* December 2013 Position Limits Proposal, 78 FR at 75729 (there may be range of spot month limits that maximize policy objectives).

[567] One commenter expressed concern that too high non-spot month limit levels could lead to a repeat of convergence problems experienced by certain contracts and that ''the imposition of all months combined limits in continuously produced non-storable commodities such as livestock . . . will reduce the liquidity needed by hedgers in deferred months who often manage their risk using strips comprised of multiple contract months.'' CL–AFBF–59730 at 3–4. One commenter requested that the Commission withdraw its proposal regarding non-spot month limits, citing, among other things, the Commission's previous approval of exchange rules lifting all-months-combined limits for live cattle contracts ''to ensure necessary deferred month liquidity.'' CL–CME–59718 at 4. Another commenter expressed concern that non-spot month limits would have a negative impact on live cattle market liquidity. CL–CMC–59634 at 12–13. *See also* CL–CME–59718 at 41.

TABLE III–B–15—SOFTS AND OTHER AGRICULTURAL CONTRACTS—NON-SPOT MONTH LIMIT LEVELS

| Contract | Previously proposed limit level [568] | Reproposed speculative limit level |
|---|---|---|
| CC | 7,100 | 10,200 |
| KC | 7,100 | 8,800 |
| CT | 8,800 | 9,400 |
| OJ | 2,900 | 5,000 |
| SB | 23,500 | 38,400 |
| SF | 1,200 | 7,000 |
| LC | 12,900 | 12,200 |

Set forth below is a summary of the impact analysis for softs and live cattle.

TABLE III–B–16—SOFTS AND OTHER AGRICULTURAL CONTRACTS—NON-SPOT MONTHS

| Core-referenced futures contract | Open interest | | | | Initial limit level | Unique persons above limit level | | Reportable persons in market—all months |
|---|---|---|---|---|---|---|---|---|
| | Year | Futures | Swaps | Total | | All months | Single month | |
| Cocoa (CC) | 1 | 240,984 | 11,257 | 252,240 | **10,200** | 12 | 7 | 682 |
| | 2 | 273,134 | 56,853 | 329,987 | | | | |
| Coffee C (KC) | 1 | 211,051 | 24,164 | 235,215 | **8,800** | 6 | * | 1,175 |
| | 2 | 223,885 | 51,846 | 275,731 | | | | |
| Cotton No. 2 (CT) | 1 | 238,580 | 35,102 | 273,682 | **9,400** | 13 | 8 | 1,000 |
| | 2 | 239,321 | 60,477 | 299,798 | | | | |
| FCOJ–A (OJ) | 1 | 16,883 | 121 | 17,004 | **5,000** | | | |
| | * | * | 242 | | | | | |
| | 2 | 16,336 | 5 | 16,341 | | | | |
| Sugar No. 11 (SB) | 1 | 1,016,271 | 211,994 | 1,228,265 | **38,400** | 14 | 9 | 874 |
| | 2 | 1,077,452 | 382,816 | 1,460,268 | | | | |
| Sugar No. 16 (SF) | 1 | 8,385 | 0 | 8,385 | **7,000** | * | 0 | 22 |
| | 2 | 9,608 | 0 | 9,608 | | | | |
| Live Cattle (LC) | 1 | 387,896 | 23,626 | 411,522 | **12,200** | 9 | * | 1,436 |
| | 2 | 350,147 | 52,330 | 402,478 | | | | |

Year 1 = July 1, 2014 to June 30, 2015. Year 2 = July 1, 2015 to June 30, 2016. Reproposed speculative position limit levels are shown in **bold**.
* Denotes fewer than 4 persons.

c. Metals

The Commission is reproposing non-spot month speculative position limit levels for the GC, SI, PL, PA, and HG core referenced futures contracts based on the 10, 2.5 percent open interest formula.[569]

[568] December 2013 Position Limits Proposal, 78 FR at 75839–40 (App. D to part 150—Initial Position Limit Levels).

[569] One commenter was concerned that applying the 10, 2.5 percent formula to open interest for gold would result in a lower non-spot month limit level than the spot month limit level, and urged the Commission to ''apply a consistent methodology to both spot and non-spot months.'' CL–WGC–59558 at 5.

TABLE III–B–17—CME METALS CONTRACTS—NON-SPOT MONTH LIMIT LEVELS

| Contract | Previously proposed limit level | Reproposed speculative limit level |
|---|---|---|
| GC | 21,500 | 19,500 |
| SI | 6,400 | 7,600 |
| PL | 5000 | 5,000 |
| PA | 5000 | 5,000 |
| HG | 5,600 | 7,800 |

Set forth below is a summary of the impact analysis for metals.[570]

TABLE III–B–18—CME METALS CONTRACTS—NON-SPOT MONTHS

| Core-referenced futures contract | Open interest | | | | Initial limit level | Unique persons above limit level | | Reportable persons in market—all months |
|---|---|---|---|---|---|---|---|---|
| | Year | Futures | Swaps | Total | | All months | Single month | |
| Gold (GC) | 1 | 618,738 | 47,727 | 666,465 | **19,500** | 19 | 17 | 1,557 |
| | 2 | 667,495 | 36,029 | 703,525 | | | | |
| Silver (SI) | 1 | 218,028 | 9,867 | 227,895 | **7,600** | 15 | 18 | 1,023 |
| | 2 | 203,645 | 3,510 | 207,155 | | | | |
| Platinum (PL) | 1 | 70,151 | 21,566 | 91,717 | **5,000** | 26 | 26 | 842 |
| | 2 | 70,713 | 2,285 | 72,997 | | | | |
| Palladium (PA) | 1 | 37,488 | 1,929 | 39,417 | **5,000** | * | * | 580 |
| | 2 | 28,276 | 823 | 29,099 | | | | |
| Copper (HG) | 1 | 170,784 | 22,859 | 193,643 | **7,800** | 19 | 12 | 1,457 |
| | 2 | 186,525 | 47,365 | 233,890 | | | | |

Year 1 = July 1, 2014 to June 30, 2015
Year 2 = July 1, 2015 to June 30, 2016
Reproposed speculative position limit levels are shown in **bold**.
* Denotes fewer than 4 persons.

d. Energy

The Commission is reproposing non-spot month speculative position limit levels for the NG, CL, HO, and RB core referenced futures contracts based on the 10, 2.5 percent open interest formula.[571]

[570] One commenter expressed concern that imposing non-spot position limits on copper would negatively affect liquidity as evidenced by the number of unique persons affected. CL–CMC–59634 at 13, n. 26. Another commenter cited the number of unique traders with all-months overages as shown in the open interest data for the GC, SI and PL contracts in the December 2013 Position Limits Proposal as an indication that ''the impact of the Commission's non-spot-month position limits is random and arbitrarily inflexible with no relationship to preventing excessive speculation or manipulation.'' CL–CME–59718 at 41.

[571] One commenter suggested deriving non-spot month limit levels for the CL, HO, and RB referenced contracts from the usage ratios for U.S. crude oil and oil products rather than open interest and expressed concern that ''unnecessarily low limits will hamper legitimate hedging activity.'' CL–Citadel–59717 at 7–8. Another commenter suggested setting limit levels based on customary position size. CL–APGA–59722 at 6. This commenter also supported setting the single month limit at two-thirds of the all months combined limit in order to relieve market congestion as traders exit or roll out of the next to expire month into the spot month. CL–APGA–59722 at 7.

TABLE III–B–19—CME ENERGY CONTRACTS—NON-SPOT MONTH LIMIT LEVELS

| Contract | Previously proposed limit level | Reproposed speculative limit level |
|---|---|---|
| NG | 149,600 | 200,900 |
| CL | 109,200 | 148,800 |
| HO | 16,100 | 21,300 |
| RB | 11,800 | 15,300 |

Set forth below is a summary of the impact analysis for energy contracts.

TABLE III–B–20—CME ENERGY CONTRACTS—NON-SPOT MONTHS

| Core-referenced futures contract | Open interest | | | | Initial limit level | Unique persons above limit level | | Reportable persons in market—all months |
|---|---|---|---|---|---|---|---|---|
| | Year | Futures | Swaps | Total | | All months | Single month | |
| Natural Gas (NG) | 1 | 4,919,841 | 2,866,128 | 7,785,969 | **200,900** | * | 0 | 1,846 |
| | 2 | 4,628,471 | 3,331,141 | 7,959,612 | | | | |
| Light Sweet Crude (CL) | 1 | 4,071,681 | 1,587,450 | 5,659,130 | **148,800** | 0 | 0 | 2,673 |
| | 2 | 4,130,131 | 1,744,137 | 5,874,268 | | | | |
| NY Harbor ULSD (HO) | 1 | 638,040 | 138,360 | 776,400 | **21,300** | 6 | * | 760 |
| | 2 | 587,796 | 65,721 | 653,518 | | | | |
| RBOB Gasoline (RB) | 1 | 448,598 | 81,822 | 530,420 | **15,300** | 8 | 7 | 837 |
| | 2 | 505,849 | 30,477 | 536,327 | | | | |

Year 1 = July 1, 2014 to June 30, 2015.
Year 2 = July 1, 2015 to June 30, 2016.
Reproposed speculative position limit levels are shown in **bold**.
* Denotes fewer than 4 persons.

6. Subsequent Levels of Limits

The Commission notes that many of the comments referenced above, regarding setting initial position limits, are also discussed below, regarding re-setting levels of limits.

a. General Procedure for Re-Setting Levels of Limits

*Commission Proposal:* The Commission proposed in § 150.2(e)(2) that it would fix subsequent levels of speculative position limits no less frequently than every two calendar years, in accordance with the procedures in § 150.2(e)(3) for spot-month limits and § 150.2(e)(3) for non-spot-month limits, discussed below.[572] The Commission proposed it would publish such subsequent levels on its Web site.

*Comments Received:* Regarding § 150.2(e)(2), commenters requested the Commission review the level of limits more frequently than every two years to address changes that may occur within the commodities markets.[573]

*Commission Reproposal:* The Commission has determined to repropose this provision as previously proposed in the December 2013 Position Limits Proposal, and reiterates that it will fix subsequent levels no less frequently than every two calendar years. The Commission is not proposing to establish a procedural requirement to reset limit levels more frequently than every two years, because as the frequency of reset increases, the burdens on market participants to update compliance systems and strategies, and on exchanges to submit deliverable supply estimates and reset exchange limit levels, also increase. The Commission believes that a two year timetable should reduce burdens on market participants while still maintaining limits based on recent market data. Should higher limit levels be desired, exchanges or market participants may petition the Commission to change limit levels within the two year period.

b. Re-setting Levels of Spot-Month Limits

*Commission Proposal:* The Commission proposed in § 150.2(e)(3) to reset each spot month limit at a level no greater than one-quarter of the estimated spot-month deliverable supply, based on the estimate of deliverable supply provided by the exchange listing the core referenced futures contract. The Commission proposed that it could, in its discretion, rely on its own estimate of deliverable supply. The Commission further proposed that, alternatively, it could set spot-month limits based on the recommended level of the exchange listing the core referenced futures contract, if lower than 25 percent of estimated deliverable supply.[574]

*Comments Received:* Commenters generally recommended the Commission enhance predictability and reduce uncertainty for market participants, by either restricting how much adjustment would be made to the position limit level, or having the discretion to not alter position limit

[572] December 2013 Position Limits Proposal, 78 FR at 75728.

[573] CL–Public Citizen–59648 at 5; CL–AFR–59711 at 2; CL–IECA–59713 at 3; CL–Better Markets–60325 at 2–3; CL–Better Markets–60401 at 19–20; CL–CMOC–59720 at 3; CL–Cota–59706 at 2; CL–RF–60372 at 3.

[574] December 2013 Position Limits Proposal, 78 FR at 75728.

levels, for example, if there have not been problems with convergence.[575]

Commenters were divided regarding the proposed methodology for computing spot month position limit levels (which is calculated by determining a figure that is no more than 25 percent of estimated deliverable supply).[576] Several commenters stated that the proposed formula for setting spot month limits based on 25 percent of deliverable supply results in spot month position limits that would be too high and may result in contract performance issues.[577] Other commenters thought the formula results in spot-month position limits that would be too low and hinder market liquidity.[578] Yet another requested that the Commission do further research to determine whether deliverable supply or open interest was a better means of setting spot month position limits, and apply the same metric (deliverable supply or open interest) to spot month limits and to non-spot month limits.[579] Several commenters recommended that the Commission consider an alternative means of limiting excessive speculation, that is, by setting position limits at a level low enough to restore a hedger majority in open interest in each core referenced futures contract.[580]

In estimating deliverable supply, some commenters recommended that the Commission include supply that is subject to long-term supply contracts, arguing that such supply can be readily made available for futures delivery.[581] One commenter recommended that the Commission permit the inclusion in the deliverable supply calculation of supplies that can be readily transported to the futures delivery location.[582] Another commenter recommended that the deliverable supply estimate should include related commodities that a DCM allows to be used to liquidate a futures position through an EFP transaction.[583] One commenter recommended that the deliverable supply estimate for natural gas should include supplies that are available at other major locations in addition to the specific futures delivery location of Erath, Louisiana, because commercials at these locations use the futures contract for hedging and price basing and basing spot month limits on a more limited delivery area would be too restrictive.[584] In estimating deliverable supply, one commenter recommended that the Commission not include supplies that do not meet delivery specifications.[585] The same commenter said that DCMs should provide documentation if including long term supply agreements in deliverable supply estimates to enable the Commission to verify the information. The commenter expressed concern about financial holding companies' ability to own, warehouse and trade physical commodities and urged the Commission to assess how such firms might affect deliverable supply.[586]

*Commission Reproposal:* The Commission is reproposing to reset each spot-month limit, in its discretion, either: Based on 25 percent of deliverable supply as estimated by an exchange listing the core referenced futures contract; to the existing spot-month position limit level (that is, not changing such level); or to the recommended level of the exchange listing the core referenced futures contract, but not greater than 25 percent of estimated deliverable supply. In the alternative, if the Commission elects to rely on its own estimate of deliverable supply, it will first publish that estimate for comment in the **Federal Register**.

Thus, the Commission accepts the commenter's recommendation that the Commission have discretion to retain current spot-month position limit levels. In this regard, the Commission provides, in reproposed § 150.2(e)(3)(ii)(B), that an exchange need not submit an estimate of deliverable supply, if the exchange provides notice to the Commission, not less than two calendar months before the due date for its submission of an estimate, that it is recommending the Commission not change the spot-month limit, and the Commission accepts such recommendation.

The Commission notes that it has long used deliverable supply as the basis for spot month position limits due to concerns regarding corners, squeezes, and other settlement-period manipulative activity. By restricting derivative positions to a proportion of the deliverable supply of the commodity, spot month position limits reduce the possibility that a market participant can use derivatives, including referenced contracts, to affect the price of the cash commodity (and vice versa). Limiting a speculative position based on a percentage of deliverable supply also restricts a speculative trader's ability to establish a leveraged position in cash-settled derivative contracts, diminishing that trader's incentive to manipulate the cash settlement price. Commenters did not provide evidence that would suggest that the open interest formula would respond more effectively to these concerns, and the Commission does not believe that using open interest would be preferable for calculating spot-month position limit levels.

In addition, setting the limit levels at no greater than 25 percent of deliverable supply has historically been effective on both the federal and exchange level to combat corners and squeezes. In the preamble to the final rules for vacated Part 151, the Commission noted that the 25 percent of deliverable supply formula appears to ''work effectively as a prophylactic tool to reduce the threat of corners and squeezes and promote convergence without compromising market liquidity.'' Commenters did not provide evidence to support claims that this historical formula is no longer effective.

In response to concerns that 25 percent of deliverable supply may result in a limit level that is too high, the Commission notes that exchanges can and often do—and are permitted under reproposed § 150.5(a) to—set limits at a level lower than 25 percent of estimated deliverable supply, which allows the exchanges to alter exchange-set limits easily based on changing market conditions.

In response to commenters' suggestion to restore a hedger majority, the Commission notes such an alternative may fail the requirements of CEA section 4a(a)(3)(B)(iv) to ensure sufficient liquidity for bona fide hedgers. Hedgers may not be transacting on opposite sides of the market simultaneously and, thus, need speculators to provide liquidity. Simply changing the proportion of hedgers in the market does not mean that the markets would operate more efficiently for bona fide hedgers. In addition, in order to adopt the commenter's suggestion, the Commission would need to reintroduce the withdrawn '03 series forms which required traders to identify which positions were speculative and which were hedging, since any entity,

[575] CL–FIA–60303 at 8, Agricultural Advisory Committee Meeting Transcript at 126–134 (Dec. 9, 2014).

[576] *E.g.,* CL–WGC–59558 at 5; CL–MFA–60385 at 4–6; CL–ISDA/SIFMA–59611 at 3, 31, 55–56, and 63–64; CL–MGEX–59610 at 2; CL–NGFA–59681 at 4–5.

[577] *See, e.g.,* CL–WGC–59558 at 5; CL–Public Citizen–60313 at 1; CL–Tri-State–59682 at 1–2; CL–AFR–59711 at 2; CL–WEED–59628 at 1; CL–Industrial Energy Consumers of America–59671 at 3; CL–CMOC–59720 at 3; CL–IATP–60394 at 2; CL–NGFA–59681 at 4–5.

[578] CL–ISDA/SIFMA–59611 at 55; CL–Armajaro–59729 at 1; CL–CAM–60097 at 3–4.

[579] CL–WGC–59558 at 5.

[580] *E.g.,* CL–IATP–60323 at 5; CL–IATP–60394 at 2; CL–RF–60372 at 3.

[581] CL–FIA–59595 at 3, 9–10; CL–NGSA–59941 at 15.

[582] CL–MFA–59606 at 18; CL–MFA–60385 at 6.

[583] CL–MSCGI–59708 at 2, 11.

[584] CL–CAM–60097 at 3–4.

[585] CL–IATP–60323 at 6.

[586] CL–IATP–60323 at 7.

even a commercial end-user, can establish speculative positions.

In response to commenters' suggestions regarding methods for estimating deliverable supply, the Commission notes that deliverable supply estimates are calculated and submitted by DCMs. Guidance for calculating deliverable supply can be found in Appendix C to part 38. Amendments to part 38 are beyond the scope of this rulemaking. However, such guidance already provides that deliverable supply calculations are estimates based on what ''reasonably can be expected to be readily available'' (including estimates of long-term supply that can be shown to be regularly made available for futures delivery).

c. Re-Setting Levels of Non-Spot-Month Limits

*Commission Proposal—General Procedure:* For setting subsequent levels of non-spot month limits no less frequently than every two calendar years, the Commission proposed in § 150.3(e)(4) to use the open interest formula: 10 percent of the first 25,000 contracts and 2.5 percent of the open interest thereafter (10, 2.5 percent formula).[587]

*Comments Received and Commission Response:* ''In order to enhance the predictability and reduce uncertainty in business planning,'' one commenter recommended that the Commission ''adjust limits gradually and by no more than a minimum percentage in one biennial cycle.'' [588] The Commission declines this suggestion because, as explained below, the Commission is reproposing a minimum non-spot month limit level of 5,000 contracts; market participants would be certain that in no circumstance would the limit level fall below that figure. Also, because exchanges can set limits at levels below the federal limit level, a change in the federal limit may not have an effect on exchange limit levels.

Several commenters recommended that the Commission review the levels of position limits more frequently than once every two years to address changes that may occur within the commodities markets.[589] In response these concerns, the Commission notes that exchanges may set limits at a level lower than the federal limits in order to more readily adapt to changing market conditions. Should higher limit levels be desired, exchanges may petition the Commission or the Commission may determine to change limit levels within the two year period. Thus, the flexibility to change limit levels more frequently than every two years is already permitted by the reproposed rules and the Commission is not changing the timeline.

One commenter recommended that the Commission ''adopt final rules that give the Commission the flexibility to increase position limits immediately or with little delay so that the market can accurately respond to external forces without violating position limits'' or, in the alternative, ''include peak open interest levels beyond the most recent two years when it determines the level of open interest on which to base position limits.[590] In response, the Commission notes that using peak open interest figures, as opposed to an average, as reproposed, may not necessarily represent an accurate portrait of current market conditions. Using the most recent two years of data is designed to ensure that the non-spot-month limit levels are set relative to the current size of the market.

Several commenters expressed the view that the proposed limits based on the open interest formula would result in limit levels that are too high and would not accomplish the goal of reducing excessive speculation.[591] In response, the Commission believes the open interest formula provides a level that is low enough to reduce the potential for excessive speculation and market manipulation without unduly impairing liquidity for bona fide hedgers. Under the rules reproposed today, both the Commission and the exchanges would have flexibility to impose non-spot month limit levels at the greater of the open interest formula, the spot month limit level, or 5,000 contracts.

Several commenters expressed the view that the proposed limits based on the open interest formula would result in limit levels for dairy contracts that are too low and would restrict hedging use by limiting liquidity.[592] The Commission responds that it is deferring the imposition of position limits on the Class III Milk contract, as discussed below.[593] The Commission also observes that reproposed § 150.9 permits market participants to apply directly to the exchanges to obtain an exemption to exceed speculative position limits.

Several commenters recommended that the Commission consider an alternative means of limiting speculative traders, by setting position limits at a level low enough to restore a hedger majority in open interest in each core referenced futures contract.[594] As discussed above, the Commission is concerned that ''restoring'' a hedger majority may not ensure sufficient liquidity for bona fide hedgers. Hedgers may not be transacting on opposite sides of the market simultaneously and, thus, need speculators to provide liquidity. Simply changing the proportion of hedgers in the market does not mean that the markets would operate more efficiently for bona fide hedgers. In addition, in order to implement this suggestion, the Commission would need to reintroduce the long defunct '03 series forms which required traders to identify which positions were speculative and which were hedging, because any entity, even a commercial end-user, can establish speculative positions.

One commenter noted that the open interest formula permits a speculator to hold a larger percentage of open interest in a smaller commodity market and thus the formula's entire rationale seems ''arbitrary . . . and . . . capricious.'' [595] The Commission acknowledges that, because of the way the 10, 2.5 percent formula works, a speculator in a market with open interest of fewer than 25,000 contracts may have a larger share of the open interest than a speculator in a market with an open interest of greater

[587] December 2013 Position Limits Proposal, 78 FR at 75729.

[588] CL–FIA–60303 at 8. This commenter did not recommend any specific percentage limitation.

[589] *E.g.,* CL–Public Citizen–59648 at 5 (annually); CL–AFR–II at 2 (greater frequency); CL–Better Markets–60325 at 2–3 (''[b]iennial updates . . . are completely inadequate''); CL–Better Markets–59716 at 34 (biennial updates values ''the input of swap dealers and their trade groups over that of commercial hedgers''); CL–CMOC–59720 at 3 (annual consultation with hedgers and end users); CL–RF–60372 at 3 (''review position limits every six months'').

[590] CL–MFA–59606 at 21.

[591] *E.g.,* CL–Tri-State–59682 at 1–2; CL–A4A–59714 at 3; CL–Better Markets–59716 at 24; CL–APGA–59722 at 3, 6; CL–AFBF–59730 at 3; CL–NGFA–59681 at 5.

[592] *E.g.,* CL–U.S. Dairy–59597 at 4, 6; CL–Hood–59582; CL–McCully–59592 at 1; CL–Rice Dairy–59601 at 1; CL–Agri-Mark–59609 at 1–2; CL–Jacoby–59622 at 1; CL–Pedestal–59630 at 2; CL–Darigold–59651 at 1–2; CL–Traditum–59655 at 1; CL–Leprino–59707 at 2; CL–IDFA–59771 at 1–2; CL–Fonterra–59608 at 1–2; CL–NCFC–59613 at 6; CL–NMPF–59936 at 2; CL–DFA–59621 at 7–8; CL–Glanbia Foods–60316 at 1; CL–Leprino Foods–59707 at 2; CL–NMPF–59936 at 2.

[593] Some commenters urged the Commission to establish an individual month position limit in Class III Milk equal to the spot month limit but no less than 3,000 contracts net, and an all-months-limit as a multiple of four times the spot month limit, to foster needed liquidity in the non-spot months. *See, e.g.,* CL–NCFC–59942 at 6. Another commenter urged an all-months-limit in Class III Milk of ten times the spot month limit for a similar reason. CL–U.S. Dairy–59597 at 4. These comments are now moot.

[594] *E.g.,* CL–IATP–60323 at 5; CL–IATP–60394 at 2; CL–RF–60372 at 3; CL–A4A–59686 at 4; CL–Better Markets–59716 at 5; CL–Better Markets–60325 at 2.

[595] CL–USCF–59644 at 3–4.

than 25,000 contracts. The Commission responds that it is by design that the 10, 2.5 percent open interest formula provides that a speculator may hold a larger percentage of total open interest in a smaller market, potentially providing liquidity for bona fide hedgers in such a smaller market. As open interest increases, the 2.5% marginal increase results in limit levels that become a progressively smaller percentage of total open interest, essentially placing a greater emphasis on deterring market manipulation and protecting the price discovery process in a larger market.

Another commenter suggested that the Commission use a 10, 5 percent open interest formula rather than a 10, 2.5 percent formula as proposed, arguing that the 10, 5 percent formula has worked well for certain agricultural futures markets and should be applied more broadly. Alternatively, this commenter said that Commission should use the 10, 5 percent formula for at least spread positions.[596] The Commission notes the 10, 2.5 percent formula has produced limit levels that should sufficiently maximize the CEA section 4a(a)(3)(B) criteria, and the Commission does not believe increasing the marginal percentage is necessary. A larger limit such as would be produced from a 10, 5 percent formula may not adequately prevent excessive speculation. In the preamble to the proposed rules, the Commission noted that the 10, 2.5 percent formula was first proposed in 1992, and the commenter has not provided sufficient justification for moving away from this established standard.

One commenter recommended that the Commission consider commodity-related ratios in establishing limits, such as the ratio between crude oil and its products, diesel (30 percent) and gasoline (50 percent), rather than on separate open interest formulas applied to each.[597] In response, the Commission notes setting limit levels based on the open interest of a related commodity may result in limit levels that are too large to be effective in the smaller commodity markets. For example, based on the levels proposed in this release in Appendix D, implementing a limit for NYMEX RBOB Gasoline equal to 50 percent of the crude oil limit, as suggested by the commenter, would result in a limit almost 10 times the size otherwise indicated by the open interest formula, and would equal almost 28 percent of total average open interest in the RBOB referenced contract. Further, hedgers with positions in multiple contracts could establish positions in various ratios without violating a position limit, provided they comply with the bona fide hedging position definition and any applicable requirements. The Commission also notes that the process in reproposed § 150.10 exempting certain spread positions may allow speculators some flexibility in inter- and intra-commodity spreads for the purpose of providing liquidity to bona fide hedgers.

One commenter suggested the Commission consider setting position limits on ''customary position size'' which had been used for setting non-spot month limits by the Commission in the past and which the commenter argues is a more effective means of curtailing large speculative positions.[598] In response, the Commission believes the 10, 2.5 percent formula has been effective in preventing excessive speculation without unduly limiting liquidity for bona fide hedgers. The Commission notes when the ''customary position size'' methodology was used to set non-spot-month limit levels, such levels were below the levels established using 10, 2.5 percent formula.

*Commission Reproposal Regarding General Procedure for Re-Setting Levels of Non-Spot Month Limits:* The Commission has determined to repropose the 10, 2.5 percent formula, generally as proposed in the December 2013 Position Limits Proposal, for the reasons discussed above. However, the Commission has determined, in response to requests by commenters requesting wheat parity, as discussed above, to provide that it may determine not to change the level of a non-spot month limit. This would permit, for example, the Commission to continue to retain a level of 12,000 contracts for the non-spot month limits in the KW and MWE contracts, even if average open interest did not exceed 405,000 contracts (which is the level that, when applying the 10, 2.5 percent formula, would result in a limit of 12,000 contracts).

*Commission Proposal for Time Periods, Data Sources, Publication and Minimum Levels for Re-Setting Levels of Non-Spot Month Limits:* Under proposed in § 150.2(e)(4)(i) and (ii), the Commission would estimate average open interest in referenced contracts using data reported for each of the last two calendar years pursuant to parts 16, 20, and/or 45.[599] The Commission also proposed under § 150.2(e)(4)(iii) to publish on the Commission's Web page estimates of average open interest in referenced contracts on a monthly basis to make it easier for market participants to estimate changes in levels of position limits.[600] Finally, the Commission proposed under § 150.2(e)(4)(iv) to establish minimum non-spot month levels of 1,000 contracts for agricultural commodity contracts and 5,000 contracts for exempt commodity contracts.

*Comments Received and Commission Response:* Regarding the time period for average open interest, as noted above, one commenter recommended that the Commission, as an alternative, ''include peak open interest levels beyond the most recent two years when it determines the level of open interest on which to base position limits.'' [601] In response, the Commission notes that using peak open interest figures, as opposed to an average, as reproposed, may not necessarily represent an accurate portrait of current market conditions.

Regarding data sources for average open interest, several commenters noted that the open interest data used by the Commission in determining the non-spot month limits was not complete since it did not include all OTC swaps data and that the Commission should correct this deficiency before it sets the limits using the open interest formula.[602] In response, the Commission notes it used futures-equivalent open interest for swaps reported under part 20, in determining the initial non-spot month limits, as discussed above, and believes this data also is acceptable for re-setting limit levels, as reproposed.

The Commission received no comments regarding publication of average open interest.

Regarding minimum levels for non-spot month limits, some commenters urged the Commission to afford itself the flexibility to set non-spot month limits at least as high as the spot-month position limit, rather than base the non-spot month limit strictly on the open interest formula in cases where the latter would result in a relatively small limit that would hinder liquidity.[603] The Commission accepts these

[596] CL–Working Group–59693 at 62.

[597] CL–Citadel–59717 at 7–8.

[598] CL–APGA–59722 at 6.

[599] December 2013 Position Limits Proposal, 78 FR at 75734.

[600] *Id.*

[601] CL–MFA–59606 at 21.

[602] *E.g.,* CL–DBCS–59569 at 6; CL–FIA–59595 at 14; CL–EEI–60386 at 11; CL–MFA–59606 at 5, 20, 22–23; CL–ISDA/SIFMA–59611 at 29, including footnote 108; CL–CMC–59634 at 13; CL–Olam–59658 at 3; CL–COPE–59662 at 22; CL–Calpine–59663 at 4; CL–Chamber–59684 at 5; CL–NFP–59690 at 20; CL–Just Energy–59692 at 4; CL–Working Group–59693 at 62; CL–Working Group–60396 at 8–10; CL–Citadel–59717 at 4–5.

[603] CL–ICE–59966 at 6; CL–U.S. Dairy–59597 at 4.

commenters' recommendation. Upon consideration of proposing minimum initial non-spot month limits, as discussed above, the Commission is removing the distinction between agricultural and exempt commodities. This change would establish a minimum non-spot month limit level of 5,000 contracts in either agricultural or exempt commodities.

*Commission Reproposal:* The Commission has determined to repropose these provisions generally as proposed in the December 2013 Position Limits Proposal, but with the changes described above to provide flexibility for a higher minimum level of non-spot month limits.

7. Deferral of Limits on Cash-Settled Core Referenced Futures Contracts

*Commission Proposal:*

The Commission proposed, but is not reproposing, positon limits on three cash-settled core referenced futures contracts: CME Class III Milk; CME Feeder Cattle; and CME Lean Hogs.[604]

*Comments Received:* Commenters raised concerns with these cash-settled contracts and how they fit within the federal position limits regime. While many of these concerns were raised in the context of the dairy industry, they apply to all three cash-settled core referenced futures contracts. Concerns raised include: (1) How to apply spot month limits in a contract that is cash-settled;[605] (2) the ''five-day rule'' for bona fide hedging;[606] and (3) the length of the spot month period.[607] Commenters contended that the Commission's rationale in the December 2013 Position Limits Proposal focused on concerns with physical-delivery contracts, which the commenters believe do not apply to cash-settled core referenced futures contracts because there is no physical delivery process and because the contracts settle to government-regulated price series (through the USDA).[608] Commenters were concerned that the Commission's ''one-size-fits-all'' approach discriminates against participants in dairy and livestock because the spot-month limit is effectively smaller compared to the separate spot-month limits for physical-delivery and cash-settled contracts in other commodities.[609] Several commenters suggested limit levels that do not follow the proposed formulae for determining limit levels for both spot and non-spot-month limits due to the unique aspects of cash-settled core referenced futures contracts, including the relatively large cash market and trading strategies not found in other core referenced futures markets.[610]

*Commission Determination:* The Commission, as part of the phased approach to implementing position limits on all physical commodity derivative contracts, is deferring action so that it may, at a later date: (1) Clarify the application of limits to cash-settled core referenced futures contracts; and (2) consider further which method to use to determine a level for a spot-month limit for a cash-settled core referenced futures contract. The Commission notes that the December 2013 Position Limits Proposal discussed spot-month limits primarily in the context of protecting the price discovery process by preventing corners and squeezes.[611] There was limited discussion of cash-settled core referenced futures contracts.[612] The Commission did not propose alternate means of calculating limit levels for cash-settled core referenced futures contracts in the December 2013 Position Limits Proposal.

*C. § 150.3—Exemptions*

1. Current § 150.3

*Statutory authority:* CEA section 4a(c)(1) exempts positions that are shown to be bona fide hedging positions, as defined by the Commission, from any Commission rule establishing speculative position limits under CEA section 4a(a).[613] In addition, CEA section 4a(a)(1) authorizes the Commission to exempt transactions normally know to the trade as ''spreads.''[614] Further, CEA section 4a(a)(7) authorizes the Commission to exempt any person, contract, or transaction from any position limit requirement the Commission establishes.[615]

*Current exemptions:* The three existing exemptions in current § 150.3(a), promulgated prior to the enactment of the Dodd-Frank Act, are part of the Commission's regulatory framework for speculative position limits.[616] First, current § 150.3(a)(1) exempts positions shown to be bona fide hedging positions from federal position limits.[617] Second, current § 150.3(a)(3) exempts spread positions between single months of a futures contract (and/or, on a futures-equivalent basis, options) outside of the spot month, provided a trader's spread position in any single month does not exceed the all-months limit.[618] Third, under current § 150.3(a)(4), positions carried for an eligible entity[619] in the separate account of an independent account controller (''IAC'')[620] that manages customer positions need not be aggregated with the other positions owned or controlled by that eligible entity (the ''IAC exemption'').[621]

[604] Each of these contracts is cash settled to a U.S. Department of Agriculture price series; Feeder Cattle and Lean Hogs settle to a CME-calculated index of daily USDA livestock prices, while Class III Milk settles to the monthly USDA Class III Milk price.

[605] CL–Rice Dairy–59960 at 1; CL–US Dairy–59597 at 3–4; CL–NMPF–59652 at 4; CL–DFA–59948 at 4–5.

[606] CL–NMPF–59652 at 5; CL–DFA–59948 at 8.

[607] CL–NGSA–59674 at 44; CL–ICE–59669 at 5–6.

[608] *See, e.g.,* CL–US Dairy–59597 at 3–4.

[609] CL–DFA–59948 at 6.

[610] CL–Rice Dairy–59601 at 1; CL–US Dairy–59597 at 3; CL–NMPF–59652 at 4; CL–DFA–59948 at 4–5.

[611] For example, the Commission stated that concerns regarding corners and squeezes are most acute in the markets for physical-delivery contracts in the spot month. December 2013 Position Limits Proposal, 78 FR at 75737.

[612] *See, e.g.,* December 2013 Position Limits Proposal 78 FR at 75688, including n. 82.

[613] 7 U.S.C. 6a(c)(1). Section 737 of the Dodd-Frank Act did not substantively change CEA section 4a(c)(1) (renumbering existing provision by inserting ''(1)'' after ''(c)'').

[614] 7 U.S.C. 6a(a)(1). Section 737 of the Dodd-Frank Act did not change the Commission's authority to exempt spreads under CEA section 4a(a)(1).

[615] 7 U.S.C. 6a(a)(7). Section 737 of the Dodd-Frank Act added CEA section 4a(a)(7). The Commission interprets CEA section 4a(a)(7) to provide the Commission with plenary authority to grant exemptive relief from position limits, consistent with the purposes of the CEA. Specifically, under Section 4a(a)(7), the Commission ''by rule, regulation, or order, may exempt, conditionally or unconditionally, any person, or class of persons, any swap or class of swaps, any contract of sale of a commodity for future delivery or class of such contracts, any option or class of options, or any transaction or class of transactions from any requirement it may establish . . . with respect to position limits.''

[616] For completeness, the Commission notes it previously provided an exemption in § 150.3(a)(2) for spreads of futures positions which offset option positions. However, the Commission removed and reserved that provision once it was rendered obsolete by the Commission determination to impose speculative limits on a trader's net position in futures and options combined, rather than separately. 58 FR 17973 at 17979 (April 7, 1993).

[617] 17 CFR 150.3(a)(1). The term bona fide hedging position is currently defined at 17 CFR 1.3(z) (2010). As discussed above, the Commission is reproposing a new definition of bona fide hedging position in § 150.1.

[618] The Commission clarifies that a spread position in this context means a short position in a single month of a futures contract and a long position in another contract month of that same futures contract, outside of the spot month, in the same crop year. The short and/or long positions may also be in options on that same futures contract, on a futures equivalent basis. Such spread positions, when combined with any other net positions in the single month, must not exceed the all-months limit set forth in current § 150.2, and must be in the same crop year. 17 CFR 150.3(a)(3).

[619] ''Eligible entity'' is defined in current 17 CFR 150.1(d).

[620] ''Independent account controller'' is defined in current 17 CFR 150.1(e).

[621] 17 CFR 150.3(a)(4). *See also* discussion of the IAC exemption in the 2016 Final Aggregation Rule.

2. Proposed § 150.3

In the December 2013 Position Limits Proposal, the Commission proposed a number of organizational and substantive amendments to § 150.3, generally resulting in an increase in the number of exemptions to speculative position limits. First, the Commission proposed to amend the three exemptions from federal speculative limits contained in current § 150.3. These previously proposed amendments would update cross references, relocate the IAC exemption and consolidate it with the Commission's separate proposal to amend the aggregation requirements of § 150.4,[622] and delete the calendar month spread provision which is unnecessary under changes to § 150.2 that would set the level of each single month position limit to that of the all-months position limit. Second, the Commission proposed to add exemptions from the federal speculative position limits for financial distress situations, certain spot-month positions in cash-settled referenced contracts, and grandfathered pre-Dodd-Frank and transition period swaps. Third, the Commission proposed to revise recordkeeping and reporting requirements for traders claiming any exemption from the federal speculative position limits.

a. Proposed Amendments to Existing Exemptions

*Proposed Rule:* In the December 2013 Position Limits Proposal, the Commission proposed to update cross-references within § 150.3 to reflect other changes in part 150. Specifically, the Commission proposed: To update references to the bona fide hedging definition to § 150.1 from § 1.3(z); to require that those filing for exemptive relief must meet the reporting requirements in part 19; and to add a cross-reference to aggregation provisions in proposed § 150.4.

The Commission also proposed to move the existing IAC exemption to § 150.4, thereby deleting the current exemption in § 150.3(a)(4). The Commission also proposed to delete the spread exemption in current § 150.3, because it noted that the proposed non-spot month limits rendered such an exemption unnecessary.[623]

In the 2016 Supplemental Position Limits Proposal, the Commission proposed to conform § 150.3(a) to accommodate processes proposed in other sections of part 150. Specifically, the Commission proposed under § 150.3(a)(1)(i) exemptions for those bona fide hedging positions that have been recognized by a DCM or SEF in accordance with proposed §§ 150.9 and 150.11. The Commission also proposed under § 150.3(a)(1)(iv) exemptions for those spread positions that have been recognized by a DCM or SEF in accordance with proposed § 150.10. Recognition of other positions exempted under proposed § 150.3(e) was re-numbered as subsection (v) from subsection (iv) of § 150.3(a)(1) of the 2013 Position Limits Proposal.

*Comments Received:* The Commission received no comments on the proposed conforming changes to § 150.3.[624] The Commission addresses comments on the IAC exemption in its final rule amending the aggregation policy under § 150.4, published separately.

*Commission Reproposal:* The Commission is reproposing these amendments as previously proposed in the December 2013 Position Limits Proposal.

b. Positions Which May Exceed Limits—§ 150.3(a)

*Proposed Rule:* In the December 2013 Position Limits Proposal, the Commission listed positions which may exceed limits in proposed § 150.3(a). Such positions included: (i) Bona fide hedging positions as defined in § 150.1; (ii) financial distress positions exempted under § 150.3(b); (iii) conditional spot month limit positions exempted under § 150.3(c); and (iv) other positions exempted under § 150.3(e). Proposed § 150.3(a) also provided that all such positions may exceed limits only if recordkeeping requirements in § 150.3(g) are met and any applicable reporting requirements in part 19 are met.

In the 2016 Supplemental Position Limits Proposal, the Commission proposed to revise § 150.3(a) to include, in addition to bona fide hedging positions as defined in § 150.1, positions that are recognized by a DCM or SEF in accordance with § 150.9 or § 150.11 as well as spread positions recognized by a DCM or SEF in accordance with § 150.10.

*Comments Received:* The Commission received many comments on the definition of bona fide hedging in § 150.1, as well as on the processes proposed in §§ 150.9–11.[625] The Commission addresses those comments in the discussion of the definition of bona fide hedging position in § 150.1, above, and in the discussion of the processes proposed in §§ 150.9–11, below. The Commission did not receive comments specific to the conforming revisions to § 150.3(a).

*Commission Reproposal:* The Commission is reproposing § 150.3(a) as previously proposed in the December 2013 Position Limits Proposal, with conforming changes consistent with the reproposed definition of a bona fide hedging position in § 150.1, which includes positions that are recognized by a DCM or SEF in accordance with reproposed § 150.9 or § 150.11, or by the Commission, and conforming changes consistent with the process for spread positions recognized by a DCM or SEF in accordance with reproposed § 150.10, or by the Commission.

c. Proposed Additional Exemptions From Position Limits

i. Financial Distress Exemption—§ 150.3(b)

*Proposed Rule:* The Commission proposed to add in § 150.3(b) an exemption from position limits for market participants in financial distress circumstances, upon the Commission's approval of a specific request.[626] For example, the Commission recognized that, in periods of financial distress, it may be beneficial for a financially sound market participant to take on the positions (and corresponding risk) of a less stable market participant. The Commission explained that it has historically provided an exemption from position limits in these types of situations in order to avoid sudden liquidations that could potentially reduce liquidity, disrupt price discovery, and/or increase systemic risk. The Commission therefore proposed to codify this historical practice.

*Comments Received:* One commenter requested the non-exclusive circumstances for the financial distress exemption be clarified by adding ''bud not limited to'' after the word ''include'' to permit other situations not listed.[627]

*Commission Reproposal:* In response to the commenter, the Commission clarifies that the circumstances under which a financial distress exemption may be claimed include, but are not limited to, the specific scenarios in the definition. However, the Commission believes that the proposed definition

[622] *See* November 2013 Aggregation Proposal. *See also* 2016 Final Aggregation Rule.

[623] Under the 2016 Supplemental Position Limits Proposal, DCMs and SEFs that are trading facilities would have authority to grant spread exemptions to both exchange and federal position limits. *See infra* discussion of §§ 150.5 and 150.10.

[624] The Commission received many comments on the changes to the bona fide hedging definition in § 150.1 and the processes for exchange recognition of exemptions in §§ 150.9–11. *See* discussion of the bona fide hedging definition, above, and of the processes in §§ 150.9–11, below.

[625] *Id.*

[626] December 2013 Position Limits Proposal, 78 FR at 75736.

[627] CL–CME–59718 at 71.

sufficiently articulates that the list of potential circumstances for claiming the financial distress exemption is non-exclusive, and, therefore, is reproposing the definition as previously proposed.

ii. Pre-Enactment and Transition Period Swaps Exemption—§ 150.3(d)

*Proposed Rule:* In the December 2013 Position Limits Proposal, the Commission proposed to provide an exemption from federal position limits for (1) pre-enactment swaps, defined as swaps entered into prior to July 21, 2010 (the date of the enactment of the Dodd-Frank Act of 2010), so long as the terms of which have not expired as of that date, and (2) transition period swaps, defined as swaps entered into during the period commencing July 22, 2010 and ending 60 days after the publication of the final position limit rules in the **Federal Register**, the terms of which have not expired as of that date. The Commission also proposed to allow both pre-enactment and transition period swaps to be netted with commodity derivative contracts acquired more than 60 days after publication of the final rules in the **Federal Register** for purposes of complying with non-spot-month position limits.[628]

*Comments Received:* One commenter suggested that ''grandfathering'' relief should be extended to pre-existing positions, and should also permit the pre-existing positions to be increased after the effective date of the limit. The commenter also suggested that the Commission should permit the risk associated with a pre-existing position to be offset through roll of a position from a prompt month into a deferred contract month.[629]

*Commission Reproposal:* The Commission declines to accept the commenter's recommendation regarding increasing positions, because allowing pre-existing positions to be increased after the effective date of the limits effectively would create a loophole for exceeding position limits. Further, the Commission declines the commenter's recommendation to permit a roll of a pre-existing position, because that would permit a market participant to extend indefinitely the holding of a speculative economic exposure in commodity derivative contracts exempt from position limits, frustrating the intent of speculative position limits. The Commission notes, however, that reproposed § 150.3(d), like the previous proposal, allows for netting of pre- and post-effective date positions, allowing a market participant to offset the risk of the position provided the offsetting position is not held into a spot month. The Commission is reproposing § 150.3(d) as proposed in the December 2013 Position Limits Proposal.

iii. Previously Granted Exemptions—§ 150.3(f)

*Proposed Rule:* The Commission proposed in the December 2013 Position Limits Proposal that exemptions previously granted by the Commission under § 1.47 for swap risk management would not apply to new swap positions entered into after the effective date of the final rule. The Commission noted that the proposed rules revoke the previously granted exemptions for risk management positions for such new swaps. Therefore, risk management positions that offset such new swaps would be subject to federal position limits, unless another exemption applied. The Commission explained that these risk management positions are inconsistent with the revised definition of bona fide hedging contained in the December 2013 Position Limits Proposal and the purposes of the Dodd-Frank Act amendments to the CEA.[630]

*Comments Received:* A number of commenters urged the Commission not to deny risk-management exemptions for financial intermediaries who utilize referenced contracts to offset the risks arising from the provision of diversified commodity-based returns to the intermediaries' clients.[631]

In contrast, other commenters noted that the proposed rules ''properly refrain'' from providing a general exemption to financial firms seeking to hedge their financial risks from the sale of commodity-related instruments such as index swaps, ETFs, and ETNs because such instruments are ''inherently speculative'' and may overwhelm the price discovery function of the derivative market.[632]

*Commission Reproposal:* As discussed above in the clarifications to the bona fide hedging position definition, the Commission now proposes to expand the relief in § 150.3(f) by: (1) Clarifying that such previously granted exemptions may apply to pre-existing financial instruments that are within the scope of existing § 1.47 exemptions, rather than only to pre-existing swaps; and (2) recognizing exchange-granted non-enumerated exemptions in non-legacy commodity derivatives outside of the spot month (consistent with the Commission's recognition of risk management exemptions outside of the spot month), and provided such exemptions are granted prior to the compliance date of the final rule, and apply only to pre-existing financial instruments as of the effective date of the final rule. These two changes are intended to reduce the potential for market disruption by forced liquidations, since a market intermediary would continue to be able to offset risks of pre-effective-date financial instruments, pursuant to previously-granted federal or exchange risk management exemptions.

iv. Non-Enumerated Hedging Positions—§ 150.3(e)

*Proposed Rule:* In the December 2013 Position Limits Proposal, the Commission noted that it previously permitted a person to file an application seeking approval for a non-enumerated position to be recognized as a bona fide hedging position under § 1.47. The Commission proposed to delete § 1.47 for several reasons described in the December 2013 Position Limits Proposal.[633]

Proposed § 150.3 provided that a person that engages in risk-reducing practices commonly used in the market, that the person believes may not be included in the list of enumerated bona fide hedging positions, may apply to the Commission for an exemption from position limits. As previously proposed, market participants would be guided in § 150.3(e) first to consult proposed Appendix C to part 150 to see whether their practices fell within a non-exhaustive list of examples of bona fide hedging positions as defined under proposed § 150.1.

A person engaged in risk-reducing practices that are not enumerated in the revised definition of bona fide hedging position in previously proposed § 150.1 may use two different avenues to apply to the Commission for relief from federal position limits: The person may request an interpretative letter from Commission staff pursuant to § 140.99 [634] concerning the applicability

[628] December 2013 Position Limits Proposal, 78 FR at 75738.

[629] CL–AMG–59709 at 2, 18–19.

[630] December 2013 Position Limits Proposal, 78 FR at 75740.

[631] CL–FIA–59595 at 5, 34–35; CL–AMG–59709 at 2, 12–15; CL–CME–59718 at 67–69.

[632] CL–Sen. Levin–59637 at 8; CL–Better Markets–60325 at 2.

[633] December 2013 Position Limits Proposal, 78 FR at 75738–9.

[634] 17 CFR 140.99 defines three types of staff letters—exemptive letters, no-action letters, and interpretative letters—that differ in scope and effect. An interpretative letter is written advice or guidance by the staff of a division of the Commission or its Office of the General Counsel. It binds only the staff of the division that issued it (or the Office of the General Counsel, as the case may

Continued

of the bona fide hedging position exemption, or the person may seek exemptive relief from the Commission under CEA section 4a(a)(7).[635]

In the 2016 Supplemental Position Limits Proposal, the Commission proposed §§ 150.9, 150.10, and 150.11 which provided alternative processes that would permit eligible DCMs and SEFs to provide relief for non-enumerated bona fide hedging positions, certain spread positions, and anticipatory bona fide hedging positions, respectively.[636] However, the Commission did not propose to alter or delete § 150.3 because the Commission determined to provide multiple avenues for persons seeking exemptive relief.

*Comments Received:* One commenter requested that the Commission provide a spread exemption from federal position limits for certain soft commodities, reasoning that there was a ''lack of fungibility of certain soft commodities . . . [because] inventories of various categories vary widely in terms of marketability over time.'' The commenter also stated that such a spread exemption would allow for effective competition for the ownership of certified inventories that in turn helps to maintain a close relationship between the cash and futures markets.[637] Another commenter recommended the Commission recognize calendar spread netting, and not place any limits on the same, because speculators provide liquidity in deferred months to hedgers and offset, in part, that exposure with shorter dated contracts.[638]

*Commission Reproposal:* Both of these comments were submitted in response to the December 2013 Position Limits Proposal, well in advance of the 2016 Supplemental Position Limits Proposal. Spread exemptions such as those described by the commenters are addressed in § 150.10, discussed below. The Commission is reproposing § 150.3(e) as previously proposed in the December 2013 Position Limits Proposal.

d. Proposed Conditional Spot Month Limit Exemption—§ 150.3(c)

Conditional spot month limit exemptions to exchange-set spot-month position limits for natural gas contracts were adopted in 2009, after the ICE submitted such an exemption as part of its certification of compliance with core principles required of exempt commercial markets (''ECMs'') on which significant price discovery contracts (''SPDCs'') were traded.[639]

As ICE developed its rules in order to comply with the ECM SPDC requirements,[640] ICE expressed concerns regarding the impact of position limits on the open interest in its LD1 contract. ICE demonstrated that as the open interest declines in the physical-delivery New York Mercantile Exchange Inc. (''NYMEX'') Henry Hub Natural Gas Futures (''NYMEX NG'') contract approaching expiration, open interest increases rapidly in the cash-settled ICE NG LD1 contract, and suggested that the ICE NG LD1 contract served an important function for hedgers and speculators who wished to recreate or hedge the NYMEX NG contract price without being required to make or take delivery. ICE stated that it believed there are ''significant and material distinctions between the design and use of'' the NYMEX NG contract and the ICE NG LD1 contract, and those distinctions were most pronounced at expiration. Further, ICE stated that, due to the size of some positions in the cash-settled ICE NG LD1 contract, the impact to the market of an equivalent limit could impair the ability for market participants to adjust their positions in an orderly fashion to come into compliance. For these reasons, ICE requested that the Commission consider an alternative to the Commission's acceptable practice that spot month position limits for the NG LD1 contract should be equivalent to the spot month position limits in the NYMEX NG contract.[641]

After discussion with both the Commission's Division of Market Oversight and NYMEX, ICE submitted and certified rule amendments implementing position limits and position accountability rules for the ICE NG LD1 contract. Specifically, ICE imposed a spot-month position limit and non-spot-month position accountability levels equal to those of the economically equivalent NYMEX NG contract. ICE also adopted a rule for a larger conditional position limit for traders who: (1) Agreed not to maintain a position in the NYMEX NG futures contract during the last three trading days, and (2) agreed to show ICE their complete book of Henry Hub related positions.[642]

In June 2009, the Commission also received self-certified rule amendments from CME Group, Inc. (''CME'') regarding position limits and position accountability levels for the cash-settled NYMEX Henry Hub Financial Last Day Futures (HH) contract and related cash-settled contracts.[643] The rules, as amended, established spot month position limits for the NYMEX HH contract as well as certain related cash-settled contracts so as to be consistent with the requirements for the SPDC contract on ICE. In the rule certification documents, CME stated that it was amending its position limits rules for the HH contract in anticipation of ICE's new rules. In February 2010, the conditional spot month limit exemptions on NYMEX and ICE went into effect.

*Proposed Rules:* In the December 2013 Position Limits Proposal, the

be), and third-parties may rely upon it as the interpretation of that staff. *See* description of CFTC Staff Letters, *available at http://www.cftc.gov/lawregulation/cftcstaffletters/index.htm.*

[635] *See supra* discussion of CEA section 4a(a)(7).

[636] *See infra* discussion of these alternative processes in § 150.9, § 150.10, and § 150.11.

[637] CL–CMC–59718 at 15.

[638] CL–Citadel–59717 at 8–9.

[639] CFTC Reauthorization Act of 2008 (''Farm Bill'', incorporated as Title XIII of the Food, Conservation and Energy Act of 2008, Public Law 110–246, 112 Stat. 1624 (June 18, 2008)) expanded the Commission's authority with respect to ECMs by creating a new regulatory category: ECMs on which significant price discovery contracts (''SPDCs'') were traded. The Farm Bill authorized the Commission to designate an ECM contract as a SPDC if the Commission determined, under criteria established in the Act, that the contract performed a significant price discovery function. When the Commission made such a determination, the ECM on which the SPDC was traded would be required to assume, with respect to that contract, all the responsibilities and obligations of a registered entity under the Commission's regulations and the Act. This process was invalidated and deleted by changes to the Act made under the Dodd-Frank Act of 2010.

[640] On March 16, 2009, the Commission adopted final rules implementing the provisions of the Farm Bill. 74 FR 12179 (March 23, 2009). These regulations became effective on April 22, 2009. Among other things, the rules established procedures by which the Commission would make and announce its determination as to whether a particular contract served a significant price discovery function. On July 24, 2009, the Commission issued an order finding that ICE's Henry Financial LD1 Fixed Price contract (''NG LD1 contract'') performed a significant price discovery function and, thus, that ICE was a registered entity with respect to the NG LD1 contract, subject to all provisions of the Act applicable to registered entities, including compliance with certain core principles. 74 FR 37988 (July 30, 2009).

As required after the designation of the NG LD1 contract as a SPDC, ICE submitted a demonstration of their compliance with the required core principles. One of the core principles with which ICE was required to comply under the Farm Bill ECM SPDC rules concerned position limits and position accountability rules for the contract(s) designated as SPDC(s). *See* Section 13201(C)(ii)(IV) of the Farm Bill (implemented in Section 2(h)(7) of the Act).

[641] *See* 17 CFR part 36, App. B, Core Principle IV(c)(3) (2010). 74 FR 12177 (April 22, 2009).

[642] ICE also imposed related aggregation, bona fide hedging, and other exemption rules for the ICE NG LD1 contract.

[643] New York Mercantile Exchange, Inc. Submission #09.103 (June 2, 2009): Notification of Amendments to NYMEX Rules 9A.27 and 9A.27A to Establish Hard Expiration Position Limits for Certain Natural Gas Financially Settled Contracts. Previously, NYMEX did not have spot-month limits on its HH contract and related cash-settled contracts.

Commission proposed a conditional spot month limit exemption for all commodities subject to federal limits under proposed § 150.2. That proposed rule was identical to the rule proposed in the Part 151 Proposal, with the exception that the December 2013 Position Limits Proposal did not include any restriction on trading in the cash market.[644] In proposing the conditional spot month limit exemption in proposed § 150.3(c), the Commission stated its preliminary belief that the current exemption in natural gas markets has served ''to further the purposes Congress articulated for position limits'' and that the exemption ''would not encourage price discovery to migrate to the cash-settled contracts in a way that would make the physical-delivery contract more susceptible to sudden price movements near expiration.'' [645] In addition, the Commission noted that it has observed repeatedly that open interest levels in physical-delivery contracts ''naturally decline leading up to and during the spot month, as the contract approaches expiration'' because ''both hedgers and speculators exit the physical-delivery contract in order to, for example, roll their positions to the next contract month or avoid delivery obligations.'' [646] The Commission also stated its preliminary belief that ''it is unlikely that the factors keeping traders in the spot month physical-delivery contract will change due solely to the introduction of a higher cash-settled limit,'' as traders participating in the physical-delivery contract in the spot month are ''understood to have a commercial reason or need to stay in the spot month.'' [647]

*Comments Received:* The Commission received many comments regarding the conditional spot month limit exemption. These comments revealed little to no consensus among market participants, exchanges, and industry groups regarding spot-month position limits in cash-settled contracts.

Several commenters supported the higher spot-month limit (or no limit at all) for cash-settled contracts, but opposed the restriction on holding a position in the physical-delivery referenced contract to obtain the higher limit for various reasons, including: The view that there is no discernible reason for the restriction in the first place; the belief that it provides a negative impact on liquidity in the physical delivery contract; and the view that it prevents commercials from taking advantage of the higher limit given their need to have some exposure in a physical delivery referenced contract during the spot month.[648]

One commenter said that the conditional spot month position limit exemption for gold is not supported by sufficient research, could decouple the cash-settled contract from the physical-delivery contract, and could lead to lower liquidity in the physical-delivery contract and higher price volatility.[649] Several commenters opposed a spot-month position limit for cash-settled contracts that is higher than the limit for physical-delivery contracts for various reasons including: The higher limit does not address the problem of excessive speculation; the higher limit would reduce liquidity in the physical-delivery contract; and the conditional limit is not restrictive enough and should include a restriction on holdings of the physical commodity as had been proposed in vacated part 151.[650]

Several commenters expressed the view that a market participant holding a trade option position, which presumably would be considered a physical delivery referenced contract, should not be precluded from using the conditional spot-month limit exemption because trade options are functionally equivalent to a forward contract and the conditional exemption does not restrict holding forwards.[651]

One commenter supported the conditional spot month limit exemption provided that the Commission modifies its proposal to allow independently-operated subsidiaries to hold positions in physical-delivery contracts if the subsidiary engages in separate and independent trading activities, shares no employees, and is not jointly directed in its trading activity with other subsidiaries by the parent company.[652]

Some commenters supported the continuation of the practice of DCMs separately establishing and maintaining their own conditional spot month limits and not aggregating cash-settled limits across exchanges and the OTC market, arguing that the resultant aggregated limit will be unnecessarily restrictive and result in lower liquidity and increased volatility.[653]

Some commenters expressed the view that the filing of daily Form 504 reports to satisfy the conditional spot month limit exemption was burdensome, and recommended less frequent reporting such as monthly reports [654] or no reporting at all.[655]

Two exchanges which currently permit a conditional spot month limit exemption, CME and ICE, have each submitted several comments regarding the exemption, some in direct response to the other exchange's comments. This back-and-forth nature of the disagreement surrounding the conditional spot month limit exemption has been significant and, on many aspects of the previously proposed exemption, the comments have been in direct opposition to each other. CME submitted a comment letter in response to the 2016 Supplemental Position Limits Proposal that reiterated its belief that the conditional limit would drain liquidity from the physical-delivery contract; [656] ICE responded that nothing in the natural gas market has suggested that the physical-delivery contract has been harmed.[657] ICE noted that CME's current conditional limit benefits CME's own cash-settled natural gas contracts; [658] CME responded that it opposes any conditional limit framework even though such opposition could work ''to the detriment of CME Group's commercial interests in certain of its cash-settled markets.'' [659] CME stated its belief that the CEA necessitates ''one-to-one limit treatment and similar exemptions'' for both physical-delivery and cash-settled contracts within a particular commodity; [660] ICE suggested that removing or reducing the conditional limit would ''disrupt present market practice.'' [661]

ICE also submitted a series of charts, using CFTC Commitment of Traders

[644] *See* December 2013 Position Limits Proposal, 78 FR at 75736–38.

[645] *Id.* at 75737.

[646] *Id.* at 75770.

[647] *Id.* at 75770, n. 782.

[648] *E.g.,* CL–FIA–59595 at 3 and 11; CL–EEI–EPSA–59602 at 9–10; CL–MFA–59606 at 5 and 19–20; CL–AIMA–59618 at 2; CL–ISDA/SIFMA–59611 at 31; CL–BG Group–59656 at 7; CL–BG Group–59937 at 5–6; CL–COPE–59662 at 23; CL–NGSA–59673 at 38–39; CL–NGSA–59941 at 3–4; CL–IECAssn–59957 at 9.

[649] CL–WGC–59558 at 4.

[650] *E.g.,* CL–Sen. Levin–59637 at 7; CL–AFR–59711 at 2; CL–A4A–59714 at 3; CL–Working Group–59693 at 59–60; CL–IECA–59713 at 3–4; CL–Better Markets–60401 at 17–18; CL–CME–59971 at 3; CL–CME–60307 at 4–5; CL–CME–60406 at 2; CL–CMOC–59720 at 3–6; CL–APGA–59722 at 8; CL–OSEC–59972 at 7; CL–RF–60372 at 3; CL–IATP–59701 at 5; CL–IATP–59704 at 6; CL–IATP–60394 at 2; CL–NGFA–59681 at 6.

[651] *E.g.,* CL–FIA–59595 at 20; CL–COPE–59662 at 23; CL–EEI–EPSA–60926 at 7, CL–EEI–Sup–60386 at 3–4; CL–Working Group–59693 at 59–60.

[652] CL–SEMP–59926 at 4–6; CL–SEMP–60384 at 5–6.

[653] *E.g.,* CL–IECAssn–59713 at 30–31; CL–ICE–59966 at 4–5; CL–ICE–59962 at 4–7.

[654] CL–EEI–EPSA–59602 at 10; CL–ICE–59669 at 7.

[655] CL–COPE–59662 at 24.

[656] CL–CME–60926 at 4.

[657] CL–ICE–61009 at 1.

[658] *Id.*

[659] CL–CME–61008 at 2.

[660] *Id.* at 3.

[661] CL–ICE–61009 at 2.

Report data, illustrating the opposite: That spot-month open interest and volume in the physical-delivery contract (the NYMEX NG) have actually increased since the introduction of the conditional spot month limit.[662]

CME stated its opposition to the conditional limits ''as a matter of statutory law,'' opining that CEA section 4(b) does not allow the imposition of the conditional limit.[663] CME believes that the conditional limit contained in the December 2013 Position Limits Proposal ''contravenes Congress's intent behind the statutory 'comparability' requirement'' in multiple ways, and that neither ICE nor the Commission has ''addressed these aspects of [CEA section 4(b)].'' [664]

ICE replied that the Commission ''has no basis to modify the current conditional limit level'' because the markets ''have functioned efficiently and effectively'' and the Commission should not ''change the status quo.'' [665] ICE continued that the conditional limit of five times the physical-delivery contract's spot-month limit ''appears to be arbitrary and likely insufficient'' and opined that the Commission has not indicated how it arrived at that figure or how such a level ''strikes the right balance between supporting liquidity and diminishing undue burdens.'' [666] ICE concluded that the conditional exemption ''must be maintained at no less than the current levels.'' [667]

*Commission Reproposal:* After taking into consideration all the comments it received regarding the conditional spot-month limit exemption, the Commission is reproposing the conditional spot-month limit exemption in natural gas markets only. The Commission believes the volume of comments regarding the conditional spot-month limit exemption indicates the importance of careful and thoughtful analysis prior to finalizing policy with respect to conditional spot-month limit exemptions in other cash-settled referenced contracts. In particular, the considerations may vary, and should be considered in relation to the particular commodity at issue. As such, the Commission believes it is prudent to proceed cautiously in expanding the conditional spot-month limit exemption beyond the natural gas markets where it is currently employed. The Commission encourages exchanges and/or market participants who believe that the Commission should extend the conditional spot-month limit exemption to additional commodities to petition the Commission to issue a rule pursuant to § 13.2 of the Commission's regulations.[668]

With respect to natural gas cash-settled referenced contracts, the reproposed rules allow market participants to exceed the position limit provided that such positions do not exceed 10,000 contracts and the person holding or controlling such positions does not hold or control positions in the spot-month natural gas physical-delivery referenced contract (NYMEX NG). Persons relying upon this exemption must file Form 504 during the spot month.[669]

The Commission observes that the conditional exemption level of 10,000 contracts is equal to five times the federal natural gas spot-month position limit level of 2,000 contracts. The conditional exemption level is also equal to the sum of the current conditional exemption levels for each of the NYMEX HH contract and the ICE NG LD1 contract. The Commission believes the level of 10,000 contracts provides relief for market participants who currently may hold or control 5,000 contracts in each of these two cash-settled natural gas futures contracts and an unlimited number of cash-settled swaps, while still furthering the purposes of the Dodd-Frank Act's amendments to CEA section 4a.

The Commission is proposing the fixed figure of 10,000 contracts, rather than the variable figure of five times the spot-month position limit level, in order to avoid confusion in the event NYMEX were to set its spot-month limit in the physical-delivery NYMEX NG contract at a level below 2,000 contracts.

The Commission provides, for informational purposes, summary statistical information that it considered in declining to extend the conditional spot-month limit exemption beyond the natural gas referenced contract. The four tables below present the number of unique persons that held positions in commodity derivative contracts greater than or equal to the specified levels, as reported to the Commission under the large trader reporting systems for futures and swaps, for the period July 1, 2014 to June 30, 2016. The table also presents counts of unique reportable persons, whether reportable under part 17 (futures and future option contracts) or under part 20 (swap contracts). The method the Commission used to analyze this large trader data is discussed above, under § 150.2.

The four tables group commodities only for convenience of presentation. In each table, the term ''25% DS'' means 25 percent of the deliverable supply as estimated by the exchange listing the core referenced futures contract and verified as reasonable by the Commission. Similarly, ''15% DS'' means 15 percent of estimated deliverable supply. An asterisk (''*'') means that fewer than four unique persons were reported. ''CME proposal'' means the level recommended by the CME Group for the spot-month limit. MGEX submitted a recommended spot-month limit level that is slightly less than 25 percent of estimated deliverable supply but did not affect the reported number of unique persons; no other exchange recommended a spot-month level of less than 25 percent of estimated deliverable supply.

For the first group of commodities, there was no unique person in the cash-settled referenced contracts whose position would have exceeded 25 percent of the exchange's estimated deliverable supply. Moreover, no unique person held a position in the cash-settled referenced contracts that would have exceeded the reproposed spot-month limits discussed under § 150.2, above, that are lower than 25 percent of the exchange's estimated deliverable supply.

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[662] *Id.* at 3–6.

[663] CL–CME–61008 at 2–3. CEA section 4(b)(1)(B)(ii)(1) imposes requirements on a foreign board of trade (''FBOT'') as a condition of providing U.S. persons direct access to the electronic trading and order-matching systems of the FBOT with respect to a contract that settles against any price of one or more contracts listed for trading on a registered entity. Such FBOT must adopt position limits for contract(s) that are ''comparable'' to the position limits adopted by the registered entity for the contract(s) against which the FBOT contract settles. 7 U.S.C. 6(b)(1)(B)(ii)(1), codified in 17 CFR 48.8(c)(1)(ii)(A).

[664] CL–CME–61008 at 3.

[665] CL–ICE–61022 at 2.

[666] *Id.*

[667] *Id.*

[668] 17 CFR 13.2.

[669] *See infra* discussion of part 19 and Form 504, below.

TABLE III–B–21—CME GROUP AND MGEX AGRICULTURAL CONTRACTS

| Core-referenced futures contract | Basis of spot-month level | Position limit level | Number of unique persons >= level | | Number of reportable persons in market | |
|---|---|---|---|---|---|---|
| | | | Spot month cash settled | Spot month physical delivery | Spot month only | All months |
| Corn | CME proposal | 600 | 0 | 36 | 1,050 | 2,606 |
| (CBOT current limit 600) | 25% DS | 900 | 0 | 20 | | |
| Oats | CME proposal | 600 | 0 | 0 | 33 | 173 |
| (CBOT current limit 600) | 25% DS | 900 | 0 | 0 | | |
| Soybeans | CME proposal | 600 | 0 | 22 | 929 | 2,503 |
| (CBOT current limit 600) | 25% DS | 1,200 | 0 | 14 | | |
| Soybean Meal | CME proposal | 720 | 0 | 14 | 381 | 978 |
| (CBOT current limit 720) | 25% DS | 2,000 | 0 | (*) | | |
| Soybean Oil | CME proposal | 540 | 0 | 21 | 397 | 1,034 |
| (CBOT current limit 540) | 25% DS | 3,400 | 0 | 0 | | |
| Wheat (CBOT) | CME proposal | 600 | 0 | 11 | 444 | 1,867 |
| (CBOT current limit 600) | 25% DS | 1,000 | 0 | 6 | | |
| Wheat (MGEX) | Parity w/CME proposal | 600 | 0 | (*) | 102 | 342 |
| (MGEX current limit 600) | Approx. 25% DS | 1,000 | 0 | (*) | | |
| Wheat (KCBT) | CME proposal | 600 | 0 | 4 | 250 | 718 |
| (KCBT current limit 600) | 25% CBOT DS | 1,000 | 0 | (*) | | |
| | 25% DS | 3,000 | 0 | (*) | | |
| Rough Rice | CME proposal | 600 | 0 | 0 | 91 | 281 |
| (CBOT current limit 600) | 25% DS | 2,300 | 0 | 0 | | |

For the second group of commodities, there was no unique person in the cash-settled referenced contracts whose position would have exceeded 25 percent of the exchange's estimated deliverable supply or, in the case of Live Cattle, the current exchange limit level of 450 contracts. Moreover, other than in the Sugar No. 11 contract, no unique person held a position in the cash-settled referenced contracts that would have exceeded 15 percent of the exchange's estimated deliverable supply. For informational purposes, the table also shows for Live Cattle that no unique person held a position in the cash-settled referenced contracts that would have exceeded 60 percent of the exchange's current spot-month limit of 450 contracts.[670]

TABLE III–B–22—OTHER AGRICULTURAL CONTRACTS AND ICE FUTURES U.S. SOFTS

| Core-referenced futures contract | Basis of spot-month level | Position limit level | Number of unique persons >= level | | Number of unique persons in market | |
|---|---|---|---|---|---|---|
| | | | Spot month cash settled | Spot month physical delivery | Spot month only | All months |
| Cotton No. 2 | 15% DS | 960 | 0 | (*) | 122 | 1,000 |
| (ICE current limit 300) | 25% DS | 1,600 | 0 | 0 | | |
| Cocoa | 15% DS | 3,300 | 0 | 0 | 164 | 682 |
| (ICE current limit 1,000) | 25% DS | 5,500 | 0 | 0 | | |
| Coffee | 15% DS | 1,440 | 0 | (*) | 336 | 1,175 |
| (ICE current limit 500) | 25% DS | 2,400 | 0 | (*) | | |
| Orange Juice | 15% DS | 1,680 | 0 | 0 | 38 | 242 |
| (ICE current limit 300) | 25% DS | 2,800 | 0 | 0 | | |
| Live Cattle | 60% Current Limit | 225 | 0 | 33 | 616 | 1,436 |
| (CME current limit 450) | Current limit * | 450 | 0 | 0 | | |
| Sugar No. 11 | 15% DS | 13,980 | (*) | 10 | 443 | 874 |
| (ICE current limit 5,000) | 25% DS | 23,300 | 0 | (*) | | |
| Sugar No. 16 | 15% DS | 4,200 | 0 | 0 | 12 | 22 |
| (ICE current limit 1,000) | 25% DS | 7,000 | 0 | 0 | | |

For the third group of energy commodities, there were a number of unique persons in the cash-settled referenced contracts whose position would have exceeded 25 percent of the exchange's estimated deliverable supply. For energy commodities other than natural gas, there were fewer than 20 unique persons that had cash-settled positions in excess of the reproposed spot-month limit levels, each based on 25 percent of deliverable supply, as discussed above under § 150.2. However, for natural gas referenced contracts, 131 unique persons had cash-settled positions in excess of the reproposed spot-month limit level of 2,000 contracts. As can be observed in the table below, only 20 unique persons had cash-settled referenced contract positions that would have exceeded the

[670] The Commission notes that 60 percent of the 450 contract spot-month limit is analogous to the counts presented for 15 percent of estimated deliverable supply. That is, 60 percent of 25 percent equals 15 percent.

reproposed natural gas conditional spot-month limit level of 10,000 contracts. Thus, a conditional spot-month limit exemption in natural gas referenced contracts potentially would provide relief to a substantial number of market participants, each of whom did not have a position that was extraordinarily large in relation to other traders' positions in cash-settled referenced contracts.

TABLE III–B–23—ENERGY CONTRACTS

| Core-referenced futures contract | Basis of spot-month level | Position limit level | Number of unique persons >= level | | Number of unique persons in market | |
|---|---|---|---|---|---|---|
| | | | Spot month cash settled | Spot month physical delivery | Spot month only | All months |
| Crude Oil, Light Sweet (WTI). | CME proposal * | 6,000 | 19 | 8 | 1,773 | 2,673 |
| (NYMEX current limit | 25% DS | 10,400 | 16 | (*) | | |
| 3,000 contracts) | 50% DS | 20,800 | (*) | 0 | | |
| Gasoline Blendstock (RBOB). | CME proposal | 2,000 | 23 | 14 | 463 | 837 |
| (NYMEX current limit | 25% DS | 6,800 | (*) | 0 | | |
| 1,000 contracts) | 50% DS | 13,600 | 0 | 0 | | |
| Natural Gas | 25% DS | 2,000 | 131 | 16 | 1,400 | 1,846 |
| (NYMEX current limit | 50% DS | 4,000 | 77 | (*) | | |
| 1,000 contracts) | Current single exchange conditional spot-month limit exemption. | 5,000 | 65 | (*) | | |
| | *Conditional spot-month limit exemption.* | *10,000* | 20 | 0 | | |
| ULSD (HO) | CME proposal | 2,000 | 24 | 11 | 470 | 760 |
| (NYMEX current limit | 25% DS | 2,900 | 15 | 5 | | |
| 1,000 contracts) | 50% DS | 5,800 | 5 | 0 | | |

* For WTI, CME Group recommended a step-down spot-month limit of 6,000/5,000/4,000 contracts in the last three days of trading.

For the fourth group of metal commodities, there were a few unique persons in the cash-settled referenced contracts whose position would have exceeded the reproposed levels of the spot-month limits, based on the CME Group's recommended levels, as discussed above under § 150.2. However, there were fewer than 20 unique persons that had cash-settled positions in excess of the reproposed spot-month limit levels for metal commodities; this is in marked contrast to the 131 unique persons who had cash-settled positions in excess of the reproposed spot-month limit for natural gas contracts. The Commission, in consideration of the distribution of unique persons holding positions in cash-settled metal commodity contracts across the 24 calendar months of its analysis, particularly in platinum,[671] is of the view that the spot-month limit level, as discussed above under § 150.2, and without a conditional spot-month limit exemption, is within the range of acceptable limit levels that, to the maximum extent practicable, may achieve the statutory policy objectives in CEA section 4a(a)(3)(B).

TABLE III–B–24—METAL CONTRACTS (COMEX DIVISION OF NYMEX)

| Core-referenced futures contract | Basis of spot-month level | Position limit level | Number of unique persons >= level | | Number of unique persons in market | |
|---|---|---|---|---|---|---|
| | | | Spot month cash settled | Spot month physical delivery | Spot month only | All months |
| Copper | CME proposal | 1,000 | 0 | (*) | 493 | 1,457 |
| (current limit 1,000) | 25% DS | 1,100 | 0 | (*) | | |
| Gold | CME proposal | 6,000 | (*) | (*) | 518 | 1,557 |
| (current limit 3,000) | 25% DS | 11,200 | 0 | 0 | | |
| Palladium | CME proposal | 100 | 6 | 14 | 164 | 580 |
| (current limit 100) | 25% DS | 900 | 0 | 0 | | |
| Platinum | CME proposal | 500 | 13 | (*) | 235 | 842 |
| (current limit 500) | 25% DS | 900 | 10 | (*) | | |
| | 50% DS | 1,800 | (*) | 0 | | |
| Silver | CME proposal | 3,000 | 0 | 0 | 311 | 1,023 |
| (current limit 1,500) | 25% DS | 5,600 | 0 | 0 | | |

[671] As can be observed in the open interest table discussed under § 150.2, above, the Commission notes that open interest in cash-settled platinum contracts was markedly lower in the second 12-month review period (year 2), than in the first 12-month review period (year 1).

e. Proposed Recordkeeping and Special Call Requirements—§ 150.3(g) and § 150.3(h)

*Proposed Rules:* As proposed in the December 2013 Position Limits Proposal, § 150.3(g) specifies recordkeeping requirements for persons who claim any exemption set forth in § 150.3. Persons claiming exemptions under previously proposed § 150.3 must maintain complete books and records concerning all details of their related cash, forward, futures, options and swap positions and transactions. Furthermore, such persons must make such books and records available to the Commission upon request under previously proposed § 150.3(h), which would preserve the ''special call'' rule set forth in current § 150.3(b). This ''special call'' rule would have required that any person claiming an exemption under § 150.3 must, upon request, provide to the Commission such information as specified in the call relating to the positions owned or controlled by that person; trading done pursuant to the claimed exemption; the commodity derivative contracts or cash market positions which support the claim of exemption; and the relevant business relationships supporting a claim of exemption.

The Commission noted that the previously proposed rules concerning detailed recordkeeping and special calls are designed to help ensure that any person who claims any exemption set forth in § 150.3 can demonstrate a legitimate purpose for doing so.[672]

*Comments Received:* The Commission did not receive any comments on the recordkeeping provisions in § 150.3(g) as proposed in the December 2013 Position Limits Proposal. With respect to previously proposed § 150.3(h), one commenter opposed the ''special call'' provision because, in the commenter's opinion, it is ''too passive.'' The commenter advocated, instead, a revision requiring persons claiming an exemption to maintain books and records on an ongoing basis and provide information to the Commission on a periodic and automatic basis, because even if the Commission lacked staff and resources to review the submitted material in real-time, Commission staff would have detailed historical data for use in compliance audits. This commenter stated that since required records are likely to be kept in an electronic format, the more frequent reporting requirement would not be considered burdensome.[673]

*Commission Reproposal:* The Commission believes the previously proposed recordkeeping and ''special call'' provisions in § 150.3(g) and § 150.3(h), respectively, are sufficient to limit abuse of exemptions without causing undue burdens on market participants. The Commission is reproposing these sections generally as proposed in the December 2013 Position Limits Proposal. The Commission is clarifying, in reproposed § 150.3(g)(2), that the bona fides of the pass-through swap counterparty may be determined at the time of the transaction or, alternatively, at such later time that the counterparty can show the swap position to be a bona fide hedging position. As previously proposed, such bona fides could only be determined at the time of the transaction, as opposed to at a later time.

*D. § 150.5—Exchange-Set Speculative Position Limits and Parts 37 and 38*

1. Background

As discussed above, the Commission currently sets and enforces position limits pursuant to its broad authority under CEA section 4a,[674] and does so only with respect to certain enumerated agricultural products.[675] As the Commission explained above and in the December 2013 Position Limits Proposal,[676] section 735 of the Dodd-Frank Act amended section 5(d)(1) of the CEA to explicitly provide that the Commission may mandate the manner in which DCMs must comply with the core principles.[677] However, Congress limited the exercise of reasonable discretion by DCMs only where the Commission has acted by regulation.[678]

The Dodd-Frank Act also amended DCM core principle 5. As amended, DCM core principle 5 requires that, for any contract that is subject to a position limitation established by the Commission pursuant to CEA section 4a(a), the DCM ''shall set the position limitation of the board of trade at a level not higher than the position limitation established by the Commission.''[679] Moreover, the Dodd-Frank Act added CEA section 5h to provide a regulatory framework for Commission oversight of SEFs.[680] Under SEF core principle 6, which parallels DCM core principle 5, Congress required that SEFs that are trading facilities adopt for each swap, as is necessary and appropriate, position limits or position accountability.[681] Furthermore, Congress required that, for any contract that is subject to a Federal position limit under CEA section 4a(a), the SEF shall set its position limits at a level no higher than the position limitation established by the Commission.[682]

2. Summary

As explained in the December 2013 Position Limits Proposal,[683] to implement the authority provided by section 735 of the Dodd-Frank Act amendments to CEA sections 5(d)(1) and 5h(f)(1), the Commission evaluated its pre-Dodd-Frank Act regulations and approach to oversight of DCMs, which had consisted largely of published guidance and acceptable practices, with the aim of updating them to conform to the new Dodd-Frank Act regulatory framework. Based on that review, and pursuant to the authority given to the Commission in amended sections 5(d)(1) and 5h(f)(1) of the CEA, which permit the Commission to determine, by rule or regulation, the manner in which boards of trade and SEFs, respectively, must comply with the core principles,[684] the Commission in its December 2013 Position Limit Proposal, proposed several updates to § 150.5 to promote compliance with DCM core principle 5 and SEF core principle 6 governing position limitations or accountability.[685]

First, the Commission proposed amendments to the provisions of § 150.5 to include SEFs and swaps. Second, the Commission proposed to codify rules and revise acceptable practices for

[672] December 2013 Position Limits Proposal, 78 FR at 75741.

[673] CL–O SEC–59972 at 5.

[674] CEA section 4a, as amended by the Dodd-Frank Act, provides the Commission with broad authority to set position limits, including an extension of its position limits authority to swaps positions. 7 U.S.C. 6a. *See supra* discussion of CEA section 4a.

[675] The position limits on these agricultural contracts are referred to as ''legacy'' limits, and the listed commodities are referred to as the ''enumerated'' agricultural commodities. This list of enumerated agricultural contracts includes Corn (and Mini-Corn), Oats, Soybeans (and Mini-Soybeans), Wheat (and Mini-wheat), Soybean Oil, Soybean Meal, Hard Red Spring Wheat, Hard Winter Wheat, and Cotton No. 2. *See* 17 CFR 150.2.

[676] *See* December 2013 Position Limits Proposal, 78 FR at 75748.

[677] Specifically, the Dodd-Frank Act amended DCM core principle 1 to include the condition that ''[u]nless otherwise determined by the Commission by rule or regulation,'' boards of trade shall have reasonable discretion in establishing the manner in which they comply with the core principles. *See* CEA section 5(d)(1)(B); 7 U.S.C. 7(d)(1)(B).

[678] *See* December 2013 Position Limits Proposal, 78 FR at 75748.

[679] *See* CEA section 5(d)(5)(B) (amended 2010), 7 U.S.C. 7(d)(5)(B).

[680] *See* CEA section 5h, 7 U.S.C. 7b–3.

[681] CEA section 5h(f)(6), 7 U.S.C. 7b–3(f)(6); *see also* December 2013 Position Limits Proposal, 78 FR at 75748.

[682] *Id.*

[683] December 2013 Position Limits Proposal, 78 FR at 75754.

[684] *See* CEA sections 5(d)(1)(B) and 5h(f)(1)(B); 7 U.S.C. 7(d)(1)(B) and 7b–3(f)(1)(B).

[685] December 2013 Position Limits Proposal, 78 FR at 75754.

compliance with DCM core principle 5 and SEF core principle 6 within amended § 150.5(a) for contracts subject to the federal position limits set forth in § 150.2. Third, the Commission proposed to codify rules and revise guidance and acceptable practices for compliance with DCM core principle 5 and SEF core principle 6 within amended § 150.5(b) for contracts not subject to the federal position limits set forth in § 150.2. Fourth, the Commission proposed to amend § 150.5 to implement uniform requirements for DCMs and SEFs that are trading facilities relating to hedging exemptions across all types of contracts, including those that are subject to federal limits. Fifth, the Commission proposed to require DCMs and SEFs that are trading facilities to have aggregation policies that mirror the federal aggregation provisions.[686]

In addition to the changes to the provisions of § 150.5 proposed in the December 2013 Position Limits Proposal, the Commission also noted that it had, in response to the Dodd-Frank Act, previously published several earlier rulemakings that pertained to position limits, including in a notice of proposed rulemaking to amend part 38 to establish regulatory obligations that each DCM must meet in order to comply with section 5 of the CEA, as amended by the Dodd-Frank Act.[687] In addition, as noted above, the Commission had published a proposal to replace part 150 with a proposed part 151, which was later finalized before being vacated.[688] In the December 2013 Position Limits Proposal, the Commission pointed out that as it was originally proposed, § 38.301 would require each DCM to comply with the requirements of part 151 as a condition of its compliance with DCM core principle 5.[689] When the Commission finalized Dodd-Frank updates to part 38 in 2012, it adopted a revised version of § 38.301 with an additional clause that requires DCMs to continue to meet the requirements of part 150 of the Commission's regulations—the current position limit regulations—until such time that compliance would be required under part 151.[690] At that time, the Commission explained that this clarification would ensure that DCMs were in compliance with the Commission's regulations under part 150 during the interim period until the compliance date for the new position limits regulations of part 151 would take effect.[691] The Commission further explained that its new regulation, § 38.301, was based on the Dodd-Frank amendments to the DCM core principles regime, which collectively would provide that DCM discretion in setting position limits or position accountability levels was limited by Commission regulations setting position limits.[692]

Similarly, as the Commission noted in the December 2013 Position Limits Proposal,[693] when in 2010 the Commission proposed to adopt a regulatory scheme applicable to SEFs, it proposed to require that SEFs establish position limits in accordance with the requirements set forth in part 151 of the Commission's regulations under proposed § 37.601.[694] The Commission pointed out that it had revised § 37.601 in the SEF final rulemaking, to state that until such time that compliance was required under part 151, a SEF may refer to the guidance and/or acceptable practices in Appendix B of part 37 to demonstrate to the Commission compliance with the requirements of SEF core principle 6.[695]

In the December 2013 Position Limits Proposal, the Commission noted that in light of the District Court vacatur of part 151, the Commission proposed to amend § 37.601 to delete the reference to vacated part 151. The amendment would have instead required that SEFs that are trading facilities meet the requirements of part 150, which would be comparable to the DCM requirement, since, as proposed in the December 2013 Position Limits Proposal, § 150.5 would apply to commodity derivative contracts, whether listed on a DCM or on a SEF that is a trading facility. At the same time, the Commission would have amended Appendix B to part 37, which provides guidance on complying with core principles, both initially and on an ongoing basis, to maintain SEF registration.[696] Since the December 2013 Position Limits Proposal required that SEFs that are trading facilities meet the requirements of part 150, the proposed amendments to the guidance regarding SEF core principle 6 reiterated that requirement. The Commission noted that for SEFs that are not trading facilities, to whom core principle 6 would not be applicable under the statutory language, part 150 should have been considered as guidance.[697]

More recently, the Commission issued the 2016 Supplemental Position Limits Proposal to revise and amend certain parts of the December 2013 Position Limits Proposal based on comments received on the December 2013 Position Limits Proposal,[698] viewpoints expressed during a Roundtable on Position Limits,[699] several Commission advisory committee meetings that each provided a focused forum for participants to discuss some aspects of the December 2013 Position Limits Proposal,[700] and information obtained in the course of ongoing Commission

[686] *Id.* Aggregation exemptions can be used, in effect, as a way for a trader to acquire a larger speculative position. As noted in the December 2013 Position Limits Proposal, the Commission believes that it is important that the aggregation rules set out, to the extent feasible, ''bright line'' standards that are capable of easy application by a wide variety of market participants while not being susceptible to circumvention. December 2013 Position Limits Proposal, 78 FR at 75754, n. 660.

[687] *See* December 2013 Position Limits Proposal, 78 FR at 75753; *see also* Core Principles and Other Requirements for Designated Contract Markets, 75 FR 80572 (Dec. 22, 2010) (''2010 Part 38 Proposed Rule'').

[688] *See supra* discussion under Part I.B (discussing the Commission's adoption of part 151,subsequently vacated).

[689] 2010 Part 38 Proposed Rule at 80585.

[690] Core Principles and Other Requirements for Designated Contract Markets, 77 FR 36611, 36639 (Jun. 19, 2012) (''Final Part 38 Rule''). The Commission mandated in final § 38.301 that, in order to comply with DCM core principle 5, a DCM must ''meet the requirements of parts 150 and 151 of this chapter, as applicable.'' *See also* 17 CFR 38.301.

[691] Final Part 38 Rule at 36639.

[692] *Id.* (discussing the Dodd-Frank amendments to the DCM core principles); *see also* CEA sections 5(d)(1) and 5(d)(5), as amended by the Dodd-Frank Act.

[693] December 2013 Position Limits Proposal, 78 FR at 75753.

[694] Core Principles and Other Requirements for Swap Execution Facilities, 76 FR 1214 (Jan. 7, 2011) (''SEF final rulemaking''). Current § 37.601 provides requirements for SEFs that are trading facilities to comply with SEF core principle 6 (Position Limits or Accountability), while the guidance to SEF core principle 6 (Position Limits or Accountability) in Appendix B to part 37, cites to part 151.

[695] Core Principles and Other Requirements for Swap Execution Facilities, 78 FR 33476 (June 4, 2013). Current § 37.601 provides requirements for SEFs that are trading facilities to comply with SEF core principle 6 (Position Limits or Accountability).

[696] Appendix B to Part 37—Guidance on, and Acceptable Practices in, Compliance with Core Principles.

[697] December 2013 Position Limits Proposal, 78 FR at 75753.

[698] Comments on the December 2013 Position Limits Proposal are accessible on the Commission's Web site at *http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1436.*

[699] A transcript of the June 19, 2014 Roundtable on Position Limits is available on the Commission's Web site at *http://www.cftc.gov/idc/groups/public/@swaps/documents/dfsubmission/dfsubmission_061914-trans.pdf.*

[700] Information regarding the December 9, 2014 and September 22, 2015 meetings of the Agricultural Advisory Committee, sponsored by Chairman Massad, is accessible on the Commission's Web site at *http://www.cftc.gov/About/CFTCCommittees/AgriculturalAdvisory/aac_meetings.* Information regarding February 26, 2015 and the July 29, 2015 meetings of the Energy & Environmental Markets Advisory Committee (''EEMAC''), sponsored by Commission Giancarlo, is accessible on the Commission's Web site at *http://www.cftc.gov/About/CFTCCommittees/EnergyEnvironmentalMarketsAdvisory/emac_meetings.*

review of SEF registration applications.[701]

In the 2016 Supplemental Position Limits Proposal, the Commission proposed to delay for exchanges that lack access to sufficient swap position information the requirement to establish and monitor position limits on swaps at this time by: (i) Adding Appendix E to part 150 to provide guidance regarding § 150.5; and (ii) revising guidance on DCM Core Principle 5 and SEF Core Principle 6 that corresponds to that proposed guidance regarding § 150.5.[702] In addition, the Commission in the 2016 Supplemental Position Limits Proposal proposed new alternative processes for DCMs and SEFs to recognize certain positions in commodity derivative contracts as non-enumerated bona fide hedges or enumerated anticipatory bona fide hedges, as well as to exempt from federal position limits certain spread positions, in each case subject to Commission review.[703] Moreover, the Commission proposed that DCMs and SEFs could recognize and exempt from exchange position limits certain non-enumerated bona fide hedging positions, enumerated anticipatory bona fide hedges, and certain spread positions.[704] To effectuate the latter proposals, the Commission proposed amendments to § 150.3 and new § 150.9, 150.10, and 150.11, as well as corresponding amendments to § 150.5(a)(2) and 150.5(b)(5).[705]

3. Discussion

As discussed in greater detail below, the Commission has determined to repropose § 150.5 largely as proposed in the December 2013 Position Limit Proposal and as revised in the 2016 Supplemental Position Limits Proposal. In addition, the Commission has determined to repropose the previously proposed amendments to § 37.601 and § 38.301.[706]

Some changes were made to § 150.5 in response to concerns raised by commenters; other changes to the reproposed regulation are to conform to changes made in other sections. For example, in reproposing § 150.5(b)(1) and (2), the Commission has determined to make certain changes to the acceptable practices for establishing the levels of individual non-spot or all-months combined position limits for futures and future option contracts that are not subject to federal limits. The changes to reproposed § 150.5(b)(1) and (2) correspond to changes to reproposed § 150.2(e)(4)(iv) discussed above, for establishing the levels of individual non-spot or all-months combined positions limits for futures and future option contracts that are subject to federal limits. Moreover, several non-substantive changes were made in response to commenter requests to provide greater clarity.[707]

The essential features of the changes to reproposed § 150.5 are discussed below.

a. Treatment of Swaps on SEFs and DCMs

*i. December 2013 Position Limits Proposal.* As explained above, CEA section 4a(a)(5), as amended by the Dodd-Frank Act, requires federal position limits for swaps that are ''economically equivalent'' to futures and options that are subject to mandatory position limits under CEA section 4a(a)(2).[708] The CEA also requires in SEF Core Principle 6 that a SEF that is a trading facility: (i) Set its exchange-set limit on swaps at a level no higher than that of the federal position limit; and (ii) monitor positions established on or through the SEF for compliance with the federal position limit and any exchange-set limit.[709] Similarly, for all contracts subject to a federal position limit, including swaps, DCMs, under DCM Core Principle 5, must set a position limit no higher than the federal limit.[710]

The December 2013 Position Limits Proposal specified that federal position limits would apply to referenced contracts,[711] whether futures or swaps, regardless of where the futures or swaps positions are established.[712] Consistent with DCM Core Principle 5 and SEF Core Principle 6, the Commission at § 150.5(a)(1) previously proposed that for any commodity derivative contract that is subject to a speculative position limit under § 150.2, a DCM or SEF that is a trading facility shall set a speculative position limit no higher than the level specified in § 150.2.'' [713]

ii. Comments Received to December 2013 Position Limits Proposal

Several comment letters on previously proposed § 150.5 recommended that the Commission not require SEFs to establish position limits.[714] Two noted that because SEF participants may use more than one derivatives clearing organization (''DCO''), a SEF may not know when a position has been offset.[715] Further, during the ongoing SEF registration process,[716] a number of

[701] Added by the Dodd-Frank Act, section 5h(a) of the CEA, 7 U.S.C. 7b–3, requires SEFs to register with the Commission. *See generally* ''Core Principles and Other Requirements for Swap Execution Facilities,'' 78 FR 33476 (Aug. 5, 2013). Information regarding the SEF application process is available on the Commission's Web site at *http://www.cftc.gov/IndustryOversight/TradingOrganizations/SEF2/sefhowto.*

[702] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38459–62. *See also* DCM Core Principle 5, Position Limitations or Accountability (contained in CEA section 5(d)(5), 7 U.S.C. 7(d)(5)) and SEF Core Principle 6, Position Limits or Accountability (contained in CEA section 5h(f)(6), 7 U.S.C. 7b–3(f)(6)).

[703] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38467–76 (providing for recognition of certain positions in commodity derivative contracts as non-enumerated bona fide hedges), at 38480–81 (providing for recognition of certain positions in commodity derivatives contracts as enumerated anticipatory bona fide hedges); and at 38476–80 (providing for exemptions from federal position limits for certain spread positions).

[704] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38482.

[705] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38504–13. The 2016 Supplemental Position Limits Proposal did not address the changes to §§ 37.601 or 38.301 proposed in the December 2013 Position Limits Proposal.

[706] The Commission did not receive any comments regarding the proposed changes to § 37.601 and § 38.301.

[707] *See* the removal of the provisions regarding excluded commodities from § 150.5(b) and their placement in a new section (c), which addresses only excluded commodities. In addition to the reorganization of the excluded commodity provisions, changes were made to those provisions to track changes made in other sections or paragraphs and to address concerns raised by commenters and confusion that became apparent in the comment letters.

[708] *See* December 2013 Position Limits Proposal, 78 FR at 75681–5 (the Commission interpret the statute to mandate that the Commission impose limits on futures, options, and swaps, in agricultural and exempt commodities).

[709] CEA section 5h(f)(6)(B), 7 U.S.C. 7b–3(f)(6) (SEF Core Principle 6B). The Commission codified SEF Core Principle 6, added by the Dodd-Frank Act, in § 37.600 of its regulations, 17 CFR 37.600. *See generally* Core Principles and Other Requirements for Swap Execution Facilities, 78 FR 33476, 33533–34 (June 4, 2013).

[710] CEA section 5(d)(5), 7 U.S.C. 7(d)(5) (DCM Core Principle 5). The Commission codified DCM Core Principle 5, as amended by the Dodd-Frank Act, in § 38.300 of its regulations, 17 CFR 38.300. *See* Core Principles and Other Requirements for Designated Contract Markets, 77 FR 36612, 36639 (June 19, 2012).

[711] Under the December 2013 Position Limits Proposal, ''referenced contracts'' are defined as futures, options, economically equivalent swaps, and certain foreign board of trade contracts, in physical commodities, and are subject to the proposed federal position limits. *See* December 2013 Position Limits Proposal, 78 FR at 75825.

[712] *See* December 2013 Position Limits Proposal, 78 FR at 75826 (previously proposed § 150.2).

[713] *See* December 2013 Position Limits Proposal, 78 FR at 75754–8.

[714] CL–CMC–59634 at 14–15, CL–FIA–60392 at 10. One comment letter stated that SEFs should be exempt from the requirement to set positions limits because SEFs are in the early stages of development and could be harmed by limits that restrict liquidity. CL–ISDA/SIFMA–59611 at 35.

[715] CL–CMC–59634 at 14–15, CL–FIA–60392 at 10.

[716] Under CEA section 5h(a)(1), no person may operate a facility for trading swaps unless the

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persons applying to become registered as SEFs told the Commission that they lack access to information that would enable them to knowledgeably establish position limits or monitor positions.[717] As the Commission observed in the 2016 Supplemental Position Limits Proposal, this information gap would also be a concern for DCMs in respect of swaps.[718]

iii. 2016 Supplemental Position Limits Proposal

As explained above, in the 2016 Supplemental Position Limits Proposal, the Commission proposed to temporarily delay for DCMs and SEFs that are trading facilities, which lack access to sufficient swap position information, the requirement to establish and monitor position limits on swaps by: (i) Adding Appendix E to part 150 to provide guidance regarding § 150.5; and (ii) revising guidance on DCM Core Principle 5 and SEF Core Principle 6 that corresponds to that guidance regarding § 150.5.[719] At that time, the Commission acknowledged that, if an exchange does not have access to sufficient data regarding individual market participants' open swap positions, then it cannot effectively monitor swap position limits, and expressed its belief that most exchanges do not have access to sufficient swap position information to effectively monitor swap position limits.[720]

In this regard, the Commission expressed its belief that an exchange would have or could have access to sufficient swap position information to effectively monitor swap position limits if, for example: (1) It had access to daily information about its market participants' open swap positions; or (2) it knows that its market participants regularly engage in large volumes of speculative trading activity, including through knowledge gained in surveillance of heavy trading activity, that would cause reasonable surveillance personnel at an exchange to inquire further about a market participant's intentions [721] or total open swap positions.[722]

The Commission noted that it is possible that an exchange could obtain an indication of whether a swap position established on or through a particular exchange is increasing a market participant's swap position beyond a federal or exchange-set limit, if that exchange has data about some or all of a market participant's open swap position from the prior day and combines it with the transaction data from the current day, to obtain an indication of the market participant's current open swap position.[723] The indication would alert the exchange to contact the market participant to inquire about that participant's total open swap position.

The Commission expressed its belief that although this indication would not include the market participant's activity transacted away from that particular exchange, such monitoring would comply with CEA section 5h(f)(6)(B)(ii). However, the Commission observed that exchanges generally do not currently have access to a data source that identifies a market participant's reported open swap positions from the prior trading day. With only the transaction data from a particular exchange, it would be impracticable, if not impossible, for that exchange to monitor and enforce position limits for swaps.[724]

The Commission also acknowledged in the 2016 Supplemental Position Limits Proposal that it has neither

facility is registered as a SEF or DCM. 7 U.S.C. 7b–3(a)(1). A SEF must comply with core principles, including Core Principle 6 regarding position limits, as a condition of registration. CEA section 5h(f)(1), 7 U.S.C. 7b–3(f)(1).

[717] For example, in a submission to the Commission under part 40 of the Commission's regulations, BGC Derivative Markets, L.P. states that ''[t]he information to administer limits or accountability levels cannot be readily ascertained. Position limits or accountability levels apply market-wide to a trader's overall position in a given swap. To monitor this position, a SEF must have access to information about a trader's overall position. However, a SEF only has information about swap transactions that take place on its own Facility and has no way of knowing whether a particular trade on its facility adds to or reduces a trader's position. And because swaps may trade on a number of facilities or, in many cases, over-the-counter, a SEF does not know the size of the trader's overall swap position and thus cannot ascertain whether the trader's position relative to any position limit. Such information would be required to be supplied to a SEF from a variety of independent sources, including SDRs, DCOs, and market participants themselves. Unless coordinated by the Commission operating a centralized reporting system, such a data collection requirement would be duplicative as each separate SEF required reporting by each information source.'' BGC Derivative Markets, L.P., Rule Submission 2015–09 (Oct. 6, 2015).

[718] 2016 Supplemental Position Limits Proposal, 81 FR at 38460.

[719] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38459–62.

[720] *Id.* at 38460. The Commission acknowledged that one SEF that may have access to sufficient swap position information by virtue of systems integration with affiliates that are CFTC registrants and shared personnel. This SEF requires that all of its listed swaps be cleared on an affiliated DCO, which reports to an affiliated SDR. 2016 Supplemental Position Limits Proposal, 81 FR at 38459; *see also* 38460, n. 32.

[721] *Id.* at 38460–61. For instance, heavy trading activity might cause an exchange to ask whether a market participant is building a large speculative position or whether the heavy trading activity is merely the result of a market participant making a market across several exchanges.

[722] *Id.* at 38461. *See* 17 CFR 45.3, 45.4, and 45.10. *See generally* CEA sections 4r (reporting and recordkeeping for uncleared swaps) and 21 (swap data repositories), 7 U.S.C. 6r and 24a, respectively. The Commission also observed that, unlike futures contracts, which are proprietary to a particular DCM and typically clear at a single DCO affiliated with the DCM, swaps in a particular commodity are not proprietary to any particular trading facility or platform. Market participants may execute swaps involving a particular commodity on or subject to the rules of multiple exchanges or, in some circumstances, OTC. Further, under the Commission regulations, data with respect to a particular swap transaction may be reported to any swap data repository (''SDR'').

[723] 2016 Supplemental Position Limits Proposal, 81 FR at 38461. The Commission observed, moreover, by way of example, that part 20 swaps data is a source that identifies a market participant's reported open swap positions from the prior trading day. So an exchange with access to part 20 swaps date could use it to add to any swap positions established on or through that exchange during the current trading day to get an indication of a potential position limit violation. Nonetheless, that market participant may have conducted other swap transactions in the same commodity, away from a particular exchange, that reduced its swap position. *Id.*

[724] *Id.* The Commission also noted that an exchange could theoretically obtain swap position data directly from market participants, for example, by requiring a market participant to report its swap positions, as a condition of trading on the exchange. The Commission observed, however, that it is unlikely that a single exchange would unilaterally impose a swaps reporting regime on market participants. *Id.* at 38461, n. 36. The Commission abandoned the approach of requiring market participants to report futures positions directly to the Commission many years ago. *Id.; see also* Reporting Requirements for Contract Markets, Futures Commission Merchants, Members of Exchanges and Large Traders, 46 FR 59960 (Dec. 8, 1981). Instead, the Commission and DCMs rely on a large trader reporting system where futures positions are reported by futures commission merchants, clearing members and foreign brokers. *See generally* part 19 of the Commission's regulations, 17 CFR part 19. *See also,* for example, the discussion of an exchange's large trader reporting system in the Division of Market Oversight Rule Enforcement Review of the Chicago Mercantile Exchange and the Chicago Board of Trade, July 26, 2013, at 24–7, available at *http://www.cftc.gov/idc/groups/public/@iodcms/documents/file/rercmecbot072613.pdf.*

Further, as noted above, exchanges do not have authority to demand swap position data from derivative clearing organizations or swap data repositories; nor do exchanges have general authority to demand market participants' swap position data from clearing members of DCOs or swap dealers (as the Commission does under part 20). 2016 Supplemental Position Limits Proposal, 81 FR at 38461, n. 36.

required any DCO[725] or SDR[726] to provide such swap data to exchanges,[727] nor provided any exchange with access to swaps data collected under part 20 of the Commission's regulations.[728]

The Commission stated that in light of the foregoing, it was proposing a delay in implementation of exchange-set limits for swaps only, and only for exchanges without sufficient swap position information.[729] After consideration of the circumstances described above, and in an effort to accomplish the policy objectives of the Dodd-Frank Act regulatory regime, including to facilitate trade processing of any swap and to promote the trading of swaps on SEFs,[730] the 2016 Supplemental Position Limits Proposal amended the guidance in the appendices to parts 37 and 38 of the Commission's regulations regarding SEF core principle 6 and DCM core principle 5, respectively. According to the 2016 Supplemental Position Limits Proposal, the revised guidance clarified that an exchange need not demonstrate compliance with SEF core principle 6 or DCM core principle 5 as applicable to swaps until it has access to sufficient swap position information, after which the guidance would no longer be applicable.[731] For clarity, the 2016 Supplemental Position Limits Proposal included the same guidance in a new Appendix E to proposed part 150 in the context of the Commission's proposed regulations regarding exchange-set position limits.

Although the Commission proposed to temporarily relieve exchanges that do not now have access to sufficient swap position information from having to set position limits on swaps, it also noted that nothing in the 2016 Supplemental Position Limits Proposal would prevent an exchange from nevertheless establishing position limits on swaps, while stating that it does seem unlikely that an exchange would implement position limits before acquiring sufficient swap position information because of the ensuing difficulty of enforcing such a limit. The Commission expressed its belief that providing delay for those exchanges that need it both preserved flexibility for subsequent Commission rulemaking and allowed for phased implementation of limitations on swaps by exchanges, as practicable.[732]

Additionally, the Commission observed that courts have authorized relieving regulated entities of their statutory obligations where compliance is impossible or impracticable,[733] and noted its view that it would be impracticable, if not impossible, for an exchange to monitor and enforce position limits for swaps with only the transaction data from that particular exchange.[734] The Commission expressed its belief that, accordingly, it was reasonable to delay implementation of this discrete aspect of position limits, only with respect to swaps position limits, and only for exchanges that lacked access to sufficient swap position information. This approach, the Commission believed, would further the policy objectives of the Dodd-Frank Act regulatory regime, including the facilitation of trade processing of swaps

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[725] Core principle M for DCOs addresses information sharing for risk management purposes, but does not address information sharing with exchanges for other purposes. CEA section 5b(c)(2)(M), 7 U.S.C. 7a–1(c)(2)(M), and § 39.22, 17 CFR 39.22. The Commission has access to DCO information relating to trade and clearing details under § 39.19, 17 CFR 39.19, as is necessary to conduct its oversight of a DCO. However, the Commission has not used its general rulemaking authority under CEA section 8a(5), 7 U.S.C. 12a(5), to require DCOs to provide registered entities access to swap information, although the Commission could impose such a requirement by rule. CEA section 5b(c)(2)(A)(i), 7 U.S.C. 7a–1(c)(2)(A)(i).

[726] An SDR has a duty to provide direct electronic access to the Commission, or a designee of the Commission who may be a registered entity (such as an exchange). CEA section 21(c)(4), 7 U.S.C. 24a(c)(4). *See* 76 FR 54538 at 54551, n. 141 (Sept. 1, 2011). However, the Commission has not designated any exchange as a designee of the Commission for that purpose. Further, the Commission has not used its general rulemaking authority under CEA section 8a(5), 7 U.S.C. 12a(5), to require SDRs to provide registered entities (such as exchanges) access to swap information, although the Commission could impose such a requirement by rule. CEA section 21(a)(3)(A)(ii), 7 U.S.C. 24a(a)(3)(A)(ii). For purposes of comparison, the Securities and Exchange Commission (''SEC'') noted with regard to security-based swaps when it finalized its rules implementing its similar provision (which it described as a ''statutory requirement that security-based SDRs conditionally provide data to certain regulators and other authorities''), ''that one or more self-regulatory organizations potentially may seek such access under this provision.'' Access to Data Obtained by Security-Based Swap Data Repositories, 81 FR 60585, 50588 (Sept. 2, 2016). The SEC estimated that ''up to 30 domestic entities potentially might enter into such MOUs or other arrangements, reflecting the nine entities specifically identified by statute or the final rules, and up to 21 additional domestic governmental entities or self-regulatory organizations that may seek access to such data.'' *Id.* at 60593.

[727] As the Commission noted in the 2016 Supplemental Position Limits Proposal, even if such information were to be made available to exchanges, the swaps positions would need to be converted to futures-equivalent positions for purposes of monitoring position limits on a futures-equivalent basis. 2016 Supplemental Position Limits Proposal, 81 FR at 38461. *See also* December 2013 Positions Limits Proposal, 78 FR at 78 FR75825 (describing the proposed definition of futures-equivalent); 2016 Supplemental Position Limits Proposal at 38461 (describing amendments to that proposed definition).

[728] 2016 Supplemental Position Limits Proposal, 81 FR at 38461. The part 20 swaps data is reported in futures equivalents, but does not include data specifying where reportable positions in swaps were established.

The Commission stated in the December 2013 Position Limits Proposal that it preliminarily had decided not to use the swaps data then reported under part 20 for purposes of setting the initial levels of the proposed single and all-months-combined positions limits due to concerns about the reliability of such data. December 2013 Position Limits Proposal, 78 FR at 75533. The Commission also stated that it might use part 20 swaps data should it determine such data to be reliable, in order to establish higher initial levels in a final rule. *Id.* at 75734.

However, as the Commission noted in the 2016 Supplemental Position Limits Proposal, the quality of part 20 swaps data does appear to have improved somewhat since the December 2013 Position Limits Proposal, although some reports continue to have significant errors. The Commission stated that it is possible that it will be able to rely on swap open positions data, given adjustments for obvious errors (*e.g.,* data reported based on a unit of measure, such as an ounce, rather than a futures equivalent number of contracts), to establish higher initial levels of non-spot month limits in a final rule. 2016 Supplemental Position Limits Proposal, 81 FR at 38461.

Moreover, the quality of the data regarding reportable positions in swaps may have improved enough for the Commission to be able to rely on it when monitoring market participants' compliance with the proposed federal position limits.

[729] *Id.*

[730] *See, e.g.,* CEA sections 5h(b)(1)(B) and 5h(e), 7 U.S.C. 7b–3(b)(1)(B) and 7b–3(e), respectively.

[731] 2016 Supplemental Position Limits Proposal, 81 FR at 38461. The Commission stated that once the guidance was no longer applicable, a DCM or a SEF would be required to file rules with the Commission to implement the relevant position limits and demonstrate compliance with Core Principle 5 or 6, as appropriate. The Commission also noted that, for the same reasons regarding swap position data discussed above in respect of CEA section 5h(f)(6)(B), the guidance proposed in the 2016 Supplemental Position Limits Proposal would temporarily relieve SEFs of their statutory obligation under CEA section 5h(f)(6)(A). *Id.*

[732] As the Commission noted above, although the 2016 Supplemental Position Limits Proposal proposed position limits relief to SEFs and to DCMs in regards to swaps, it did not propose any alteration to the definition of referenced contract (including economically equivalent swaps) that was proposed in December 2013. *See also* December 2013 Position Limits Proposal, 78 FR at 75825.

[733] 2016 Supplemental Position Limits Proposal, 81 FR at 38462. *See also id.* at n. 44 (*See, e.g., Ass'n of Irritated Residents* v. *EPA,* 494 F.3d 1027, 1031 (D.C. Cir. 2007) (allowing regulated entities to enter into consent agreements with EPA—without notice and comment—that deferred prosecution of statutory violation until such time as compliance would be practicable); *Catron* v. *County Bd. Of Commissioners* v. *New Mexico Fish & Wildlife Serv.,* 75 F.3d 1429, 1435 (10th Cir.1966) (stating that 'Compliance with [the National Environmental Protection Act] is excused when there is a statutory conflict with the agency's authorizing legislation that prohibits or renders compliance impossible.' ")). The Commission noted, moreover, that ''it is axiomatic that courts will avoid reading statutes to reach absurd or unreasonable consequences'' (citing, as an example, *Griffin* v. *Oceanic Contractors, Inc.,* 458 U.S. 564 (1982)), and pointed out that to require an exchange to monitor position limits on swaps, when it currently has extremely limited visibility into a market participant's swap position, was, arguably, absurd and certainly appeared unreasonable. 2016 Supplemental Position Limits Proposal, 81 FR at 38462, n. 44.

[734] *Id.* at 38462.

and the promotion of trading swaps on SEFs. Finally, the Commission noted that while this approach would delay the requirement for certain exchanges to establish and monitor exchange-set limits on swaps, under the December 2013 Position Limits Proposal, federal position limits would apply to swaps that are economically equivalent to futures contracts subject to federal position limits.[735]

iv. Comments Received to 2016 Supplemental Position Limits Proposal

Several commenters addressed the Commission's proposed guidance on exchange-set limits on swaps.[736]

Regarding insufficient swap data, four commenters agreed that SEFs and DCMs lack access to sufficient swap position data to set exchange limits on swaps, and as such, the commenters support the Commission's decision to delay the position limit monitoring requirements for SEFs that are trading facilities and DCMs.[737] In addition, one commenter recommended that the Commission provide notice for public comments prior to implementing any determination that a DCM or SEF has access to sufficient swap position data to set exchange limits on swaps.[738] Further, two commenters recommended that the Commission identify a plan, to address the insufficient data issues, that goes beyond ''simply exempting affected exchanges.''[739]

On the other hand, one commenter asserted that there should be no delay in implementing position limits for swaps because, according to the commenter, the Commission has access to sufficient swap data it needs to implement position limits.[740]

v. Commission Determination

The Commission has determined to repropose the treatment of swaps and SEFs as previously proposed in the 2016 Supplemental Position Limits Proposal for the reasons given above.[741]

Regarding the comments recommending that the Commission identify a plan to address the insufficient data issues that goes beyond ''simply exempting affected exchanges,'' the Commission may consider granting DCMs and SEFs, as self-regulatory organizations, access to part 20 data or SDR data at a later time.

In addition, regarding the comment that the Commission already has access to sufficient swap data in order to implement position limits, the Commission points out that it proposes to adopt a phased approach to updating its position limits regime.[742] In conjunction with this phased approach, the Commission believes that at this time it should limit its implementation of position limits for swaps to those that are referenced contracts.

b. § 150.5(a)—Requirements and Acceptable Practices for Commodity Derivative Contracts That Are Subject to Federal Position Limits

i. December 2013 Position Limits Proposal

Several requirements were added to § 150.5(a) in the December 2013 Position Limits Proposal to which a DCM or SEF that is a trading facility must adhere when setting position limits for contracts that are subject to the federal position limits listed in § 150.2.[743] Previously proposed § 150.5(a)(1) specified that a DCM or SEF that lists a contract on a commodity that is subject to federal position limits must adopt position limits for that contract at a level that is no higher than the federal position limit.[744] Exchanges with cash-settled contracts price-linked to contracts subject to federal limits would also be required to adopt those limit levels.

Previously proposed § 150.5(a)(3) would have required a DCM or SEF that is a trading facility to exempt from speculative position limits established under § 150.2 a swap position acquired in good faith in any pre-enactment and transition period swaps, in either case as defined in § 150.1.[745] However, previously proposed § 150.5(a)(3) would allow a person to net such a pre-existing swap with post-effective date commodity derivative contracts for the purpose of complying with any non-spot-month speculative position limit. Under previously proposed § 150.5(a)(4)(i), a DCM or SEF that is a trading facility must require compliance with spot month speculative position limits for pre-existing positions in commodity derivatives contracts other than pre-enactment or transition period swaps, while previously proposed § 150.5(a)(4)(ii) provides that a non-spot-month speculative position limit established under § 150.2 would not apply to any commodity derivative contract acquired in good faith prior to the effective date of such limit.[746] As proposed in the December 2013 Position Limits Proposal, however, such a pre-existing commodity derivative contract position must be attributed to the person if the person's position is increased after the effective date of such limit.[747]

Under the December 2013 Position Limits Proposal, the Commission had proposed to require DCMs and SEFs that are trading facilities to have aggregation polices that mirror the federal aggregation provisions.[748] Therefore,

[735] *Id.*

[736] *E.g.,* CL–FIA–60937 at 1,6; CL–WMBA–60945 at 1–2; CL–AFR–60953 at 2; CL–RER2–60962 at 1; CL–Better Markets–60928 at 6.

[737] CL–FIA–60937 at 2, 5–6; CL–WMBA–60945 at 1–2; CL–AFR–60953 at 2; CL–RER2–60962 at 1.

[738] CL–FIA–60937 at 2, 5–6.

[739] CL–AFR–60953 at 2; CL–RER2–60962 at 1.

[740] CL–Better Markets–60928 at 6.

[741] For purposes of clarity, the Commission is reproposing the guidance to provide for a temporarily delay for DCMs and SEFs that are trading facilities that lack access to sufficient swap position information the requirement to establish and monitor position limits on swaps by reproposing as proposed in the 2016 Supplemental Position Limits Proposal: (i) Appendix E to Part 150 to provide guidance regarding reproposed § 150.5; and (ii) guidance on DCM Core Principle 5 and SEF Core Principle 6 that corresponds to that reproposed guidance regarding § 150.5.

[742] As the Commission noted in the December 2013 Position Limits Proposal, ''a phased approach will (i) reduce the potential administrative burden by not immediately imposing position limits on all commodity derivative contracts in physical commodities at once, and (ii) facilitate adoption of monitoring policies, procedures and systems by persons not currently subject to positions limits (such as traders in swaps that are not significant price discovery contracts).'' 78 FR 75680.

[743] As discussed above, 17 CFR 150.2 provides limits for specified agricultural contracts in the spot month, individual non-spot months, and all-months-combined.

[744] As previously proposed, § 150.5(a)(1) is in keeping with the mandate in core principle 5 as amended by the Dodd-Frank Act. *See* CEA section 5(d)(1)(B), 7 U.S.C. 7(d)(1)(B). SEF core principle 6 parallels DCM core principle 5. *Compare* CEA section 5h(f)(5), 7 U.S.C. 7b–3(f)(5) with CEA section 5(d)(5), 7 U.S.C. 7(d)(5).

[745] The Commission previously proposed to exercise its authority under CEA section 4a(a)(7) to exempt pre-Dodd-Frank and transition period swaps from speculative position limits (unless the trader elected to include such a position to net with post-effective date commodity derivative contracts). Such a pre-existing swap position would be exempt from initial spot month speculative position limits. December 2013 Position Limits Proposal, 78 FR at 75756, n. 674.

[746] *See* previously proposed 150.5(a)(4)(ii). *See also* CEA section 22(a)(5)(B), added by section 739 of the Dodd-Frank Act.

[747] *See* previously proposed 150.5(a)(4)(ii). Notwithstanding any pre-existing exemption adopted by a DCM or SEF that applied to speculative position limits in non-spot months, under the December 2013 Position Limits Proposal, a person holding pre-existing commodity derivative contracts (except for pre-existing swaps as described above) would be required to comply with spot month speculative position limits. However, nothing in previously proposed § 150.5(a)(4) would override the exclusion of pre-Dodd-Frank and transition period swaps from speculative position limits. December 2013 Position Limits Proposal, 78 FR at 75756, n. 675.

[748] December 2013 Position Limits Proposal, 78 FR at 75754, 75756. As noted above, aggregation exemptions can be used, in effect, as a way for a trader to acquire a larger speculative position, and the Commission believes that it is important that the aggregation rules set out, to the extent feasible, ''bright line'' standards that are capable of easy application by a wide variety of market participants while not being susceptible to circumvention. The December 2013 Position Limits Proposal also noted that ''. . . position aggregation exemptions, if not

previously proposed § 150.5(a)(5) required DCMs and SEFs that are trading facilities to have aggregation rules that conformed to the uniform standards listed in § 150.4.[749] As noted in the December 2013 Position Limits Proposal, aggregation policies that vary from exchange to exchange would increase the administrative burden on a trader active on multiple exchanges, as well as increase the administrative burden on the Commission in monitoring and enforcing exchange-set position limits.[750]

A DCM or SEF that is a trading facility would have continued to be free to enforce position limits that are more stringent that the federal limits. The Commission clarified in the December 2013 Position Limits Proposal that federal spot month position limits do not to apply to physical-delivery contracts after delivery obligations are established.[751] Exchanges generally prohibit transfer or offset of positions once long and short position holders have been assigned delivery obligations. Previously proposed § 150.5(a)(6) clarified acceptable practices for a DCM or SEF that is a trading facility to enforce spot month limits against the combination of, for example, long positions that have not been stopped, stopped positions, and deliveries taken in the current spot month.[752]

ii. Comments Received to December 2013 Position Limits Proposal Regarding Proposed § 150.5(a)

One commenter recommended that exchanges be required to withdraw their position accountability and position limit regimes in deference to any federal limits and to conform their position limits to the federal limits so that a single regime will apply across exchanges.[753]

Two commenters recommended that the Commission clarify that basis contracts would be excluded from exchange-set limits in order to provide consistency since such contracts are excluded from the Commission's definition of referenced contract and thus are not subject to Federal limits.[754]

One commenter recommended that DCMs and SEFs that are trading facilities be given more discretion, particularly with respect to non-referenced contracts, over aggregation requirements.[755]

iii. 2016 Supplemental Position Limits Proposal

In the 2016 Supplemental Position Limits Proposal, the Commission proposed to amend § 150.5(a)(2) as it was proposed in the December 2013 Position Limits Proposal.[756] The amendments would permit exchanges to recognize non-enumerated bona fide hedging positions under § 150.9, to grant spread exemptions from federal limits under § 150.10, and to recognize certain enumerated anticipatory bona fide hedging positions under § 150.11, each as contained in the 2016 Supplemental Position Limits Proposal. In conjunction with those amendments, the Commission proposed corresponding changes to § 150.3 and § 150.5(a)(2).

For example, § 150.5(a)(2)(i), as proposed in the December 2013 Position Limits Proposal, required that any exchange rules providing for hedge exemptions for commodity derivatives contracts subject to federal position limits conform to the definition of bona fide hedging position as defined in the amendments to § 150.1 contained in the December 2013 Position Limits Proposal. But because the 2016 Supplemental Position Limits Proposal incorporated the bona fide hedging position definition and provided for spread exemptions in 150.3(a)(1)(i), the 2016 Supplemental Position Limits Proposal proposed instead to cite to § 150.3 in § 150.5(a)(2).[757] Similarly, the application process provided for in § 150.5(a)(2) was amended to conform to the requirement in proposed § 150.10 and § 150.11 that exchange rules providing for exemptions for commodity derivatives contracts subject to federal position limits require that traders reapply on at least an annual basis. In addition, the changes to § 150.5(a)(2) clarified that exchanges may deny an application, or limit, condition, or revoke any exemption granted at any time.

Similarly, the 2016 Supplemental Position Limits Proposal amended previously proposed § 150.5(b) to require that exchange rules provide for recognition of a non-enumerated bona fide hedge ''in a manner consistent with the process described in § 150.9(a).'' Addressing the granting of spread exemptions for contracts not subject to federal position limits, the 2016 Supplemental Position Limits Proposal integrates in the standards of CEA section 4a(a)(3), providing that exchanges should take into account those standards when considering whether to grant spread exemptions. Finally, the 2016 Supplemental Position Limits Proposal clarified that for excluded commodities, the exchange can grant certain exemptions provided under paragraphs § 150.5(b)(5)(i) and (b)(5)(ii) in addition to the risk management exemption previously proposed in the December 2013 Position Limits Proposal.[758]

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uniform with the Commission's requirements, may serve to permit a person to obtain a larger position on a particular DCM or SEF than would be permitted under the federal limits. For example, if an exchange were to grant an aggregation position to a corporate person with aggregate positions above federal limits, that exchange may permit such person to be treated as two or more persons. The person would avoid violating exchange limits, but may be in violation of the federal limits. The Commission believes that a DCM or SEF, consistent with its responsibilities under applicable core principles, may serve an important role in ensuring compliance with federal positions limits and thereby protect the price discovery function of its market and guard against excessive speculation or manipulation. In the absence of uniform . . . position aggregation exemptions, DCMs or SEFs may not serve that role. December 2013 Position Limits Proposal, 78 FR at 75754. *See also* 2016 Final Aggregation Rule (regarding amendments to 150.4, which were approved by the Commission in a separate release concurrently with this reproposed rulemaking).

[749] Under the December 2013 Position Limits Proposal, 17 CFR 150.5(g) would be replaced with previously proposed § 150.5(a)(5) which referenced 17 CFR 150.4 as the regulation governing aggregation for contracts subject to federal position limits.

[750] December 2013 Position Limits Proposal, 78 FR at 75755.

[751] December 2013 Position Limits Proposal, 78 FR at 75756. The Commission stated that, therefore, federal spot month position limits do not apply to positions in physical-delivery contracts on which notices of intention to deliver have been issued, stopped long positions, delivery obligations established by the clearing organization, or deliveries taken. *Id.* at 75756, n. 678.

[752] *Id.* at 75756. The December 2013 Position Limits Proposal noted, for example, that an exchange might restrict a speculative long position holder that otherwise would obtain a large long position, take delivery, and seek to re-establish a large long position in an attempt to corner a significant portion of the deliverable supply or to squeeze shorts. Previously proposed § 150.5(b)(9) set forth the same acceptable practices for contracts not subject to federal limits. *Id.* at 75756, n. 679.

[753] CL–DBCS–59569 at 4.

[754] CL–FIA–59595 at 41; CL–Nodal-59695 at 3.

[755] CL–AMG–59709 at 2, 10–11.

[756] As noted above, the changes to § 150.3 as proposed in the December 2013 Position Limits Proposal would have provided for recognition of enumerated bona fide hedge positions, but would not have exempted any spread positions from federal limits. For any commodity derivative contracts subject to federal position limits, § 150.5(a)(2) as proposed in the December 2013 Position Limits Proposal would have established requirements under which exchanges could recognize exemptions from exchange-set position limits, including hedge exemptions and spread exemptions. *See also* 2016 Supplemental Position Limits Proposal, 81 FR at 38482.

[757] As proposed in the 2016 Supplemental Position Limits Proposal, § 150.5(a)(2)(i) provides that a DCM or SEF that is a trading facility ''may grant exemptions from any speculative position limits it sets under paragraph (a)(1) of this section, provided that such exemptions conform to the requirements specified in § 150.3.''

[758] *See* § 150.5(b)(5)(D) (stating that for excluded commodities, a DCM or SEF may grant, pursuant to

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iv. Comments Received on the 2016 Supplemental Position Limits Proposal Regarding § 150.5(a)

While comments were submitted on the 2016 Supplemental Position Limits Proposal that addressed the proposed changes to the definitions under § 150.1, as well as to the proposed exchange processes for recognition of non-enumerated bona fide hedges and anticipatory hedges, and for granting spreads exemptions under proposed §§ 150.9, 150.11, and 150.10, respectively, all of which indirectly affect § 150.5(a), very few comments specifically addressed § 150.5(a). Comments received on the 2016 Supplemental Position Limits Proposal regarding the other sections are addressed in the discussions of those sections.[759]

One commenter urged the Commission to allow exchanges to maintain their current authority to set speculative limits for both spot month and all-months combined limits below federal limits to ensure that convergence continues to occur.[760]

While the Commission's retention of what is often referred to as the five-day rule [761] was included only in the revised definition of bona fide hedging position under § 150.1,[762] several commenters addressed the five-day rule in the context of § 150.5 as proposed in the 2016 Supplemental Position Limits Proposal.[763] According to the commenters, the decision of whether to apply the five-day rule to a particular contract should be delegated to the exchanges because the exchanges are in the best position to evaluate facts and circumstances, and different markets have different dynamics and needs.[764] In addition, one commenter requested that the Commission specifically authorize exchanges to grant bona fide hedging position and spread exemptions during the last five days of trading or less.[765] Two commenters suggested, as an alternative approach if the five-day rule remains, that the Commission instead rely on tools available to exchanges to address concerns, such as exchanges requiring gradual reduction of the position (''step down'' requirements) or revoking exemptions to protect the price discovery process in core referenced futures contracts approaching expiration.[766] Another commenter argued that in spite of any five-day rule that is adopted, exchanges should be allowed to recognize non-enumerated bona fide hedging exemptions during the last five trading days for enumerated strategies that are otherwise subject to the five-day rule and the discretion to grant exemptions for hedging strategies that would otherwise be subject to the five-day rule.[767]

One issue raised by several commenters [768] that did not directly address § 150.5 concerns the application procedures in §§ 150.9(a)(4), 150.10(a)(4), and 150.11(a)(3), which require market participants to apply for recognition or an exemption in advance of exceeding the limit.[769] For example, one commenter requested the insertion of a provision permitting exchanges to recognize exemptions retroactively due to ''unforeseen hedging needs''; this commenter also stated that certain exchanges currently utilize a similar rule and it is ''critical in reflecting commercial hedging needs that cannot always be predicted in advance.'' [770] Another commenter requested that the Commission allow exchanges to recognize a bona fide hedge exemption for up to a five-day retroactive period in circumstances where market participants need to exceed limits to address a sudden and unforeseen hedging need.[771] That commenter stated that CME and ICE currently provide mechanisms for such recognition, which are used infrequently but are nonetheless important. According to that commenter, ''[t]o ensure that such allowances will not diminish the overall integrity of the process, two effective safeguards under the current exchange-administered processes could continue to be required. First, the exchange rules could continue to require market participants making use of the retroactive application to demonstrate that the applied-for hedge was required to address a sudden and unforeseen hedging need. . . . Second, if the emergency hedge recognition is not granted, the exchange rules could continue to require the applicant to immediately unwind its position and also deem the applicant to have been in violation for any period in which its position exceeded the applicable limits.[772] While these comments address other sections, the Commission will respond to these comments in explaining its reproposal of § 150.5.

v. Commission Determination Regarding § 150.5(a)

The Commission has determined to repropose § 150.5(a) as proposed in the 2016 Supplemental Position Limits Proposal for the reasons provided above with some changes, as detailed below.[773]

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rules submitted to the Commission, ''the exemptions under paragraphs (b)(5)(i) and (b)(5)(ii)(A) through (C)''). While the December 2013 Position Limits Proposal numbered the provisions applicable to excluded commodities as § 150.5(b)(5)(ii)(E), the 2016 Supplemental Position Limits Proposal renumbered the provision as § 150.5(b)(5)(ii)(D).

[759] One example of an issue raised by several commenters concerns the application procedures in §§ 150.9(a)(4), 150.10(a)(4), and 150.11(a)(3), which requires market participants to apply for recognition or an exemption in advance of exceeding the limit. *See, e.g.,* CL–FIA–60937 at 4, 13; CL–CME–60926 at 12; CL–ICE–60929 at 11, 20–21; CL–NCGA–NGSA–60919 at 10–11; CL–EEI–EPSA–60925 at 4; CL–ISDA–60931 at 13; and CL–CMC–60950 at 3. For example, ICE requested the insertion of a provision for exchanges to recognize exemptions retroactively due to ''unforeseen hedging needs,'' and also stated that certain exchanges currently utilize a similar rule and it is ''critical in reflecting commercial hedging needs that cannot always be predicted in advance.'' CL–ICE–60929 at 11.

[760] CL–NGFA–60941 at 2.

[761] The Commission's current definition of ''bona fide hedging transactions and positions,'' under § 1.3(z), applies the ''five-day rule'' in § 1.3(z)(2) subsections (i)(B), (ii)(C), (iii), and (iv). Under those sections of the ''five-day rule,'' no such positions and transactions were maintained in the five last days of trading. *See* § 1.3(z).

[762] As noted in the December 2013 Position Limits Proposal (which did not change in the 2016 Supplemental Position Limits Proposal), the Commission previously proposed to delete § 1.3(z) and replace it with a new definition in § 150.1 of ''bona fide hedging position.'' And, as noted above, the December 2013 Position Limits Proposal retained the five-day rule. The previously proposed definition was built on the Commission's history and was grounded for physical commodities in the new requirements of CEA section 4a(c)(2) as amended by the Dodd-Frank Act. December 2013 Position Limits Proposal, 78 FR at 75706.

[763] *E.g.,* CL–NCGA–ASA–60917 at 1–2; CL–CME–60926 at 14–15; CL–ICE–60929 at 7–8; CL–ISDA–60931 at 11; CL–CCI–60935 at 3; CL–MGEX–60936 at 4; CL–Working Group–60947 at 5, 7–9; CL–IECAssn–60949 at 7–9; CL–CMC–60950 at 9–14; CL–NCC–ACSA–60972 at 2. No comments on the December 2013 Position Limits Proposal specifically addressed the ''five-day rule'' in the context of § 150.5.

[764] *See, e.g,* CL–ISDA–60931 at 10; CL–CCI–60935 at 3; CL–MGEX–60936 at 11; CL–Working Group–60947 at 7–9.

[765] CL–CMC–60950 at 11–12.

[766] CL–Working Group–60947 at 8; CL–IECAssn–60949 at 7–9.

[767] CL–CME–60926 at 6, 8.

[768] CL–FIA–60937 at 4, 13; CL–CME–60926 at 12; CL–ICE–60929 at 11, 20–21; CL–NCGA–NGSA–60919 at 10–11; CL–EEI–EPSA–60925 at 4; CL–ISDA–60931 at 13; and CL–CMC–60950 at 3.

[769] *See* 150.9(a)(4) (requiring each person intending to exceed position limits to, among other things, ''receive notice of recognition from the designated contract market or swap execution facility of a position as a non-enumerated bona fide hedge in advance of the date that such position would be in excess of the limits then in effect pursuant to section 4a of the Act.'')

[770] CL–ICE–60929 at 11.

[771] CL–NCGA–NGSA–60919 at 10–11.

[772] *Id.* at 11 (footnote omitted).

[773] For example, the Commission is reproposing the following sections as previously proposed without change for the reasons provided above: § 150.5(a)(1); § 150.5(a)(3) (Pre-enactment and transition period swap positions), § 150.5(a)(4) (Pre-existing positions), and § 150.5(a)(6) (Additional acceptable practices); no substantive comments were received regarding those sections.

Although the Commission is reproposing § 150.5(a)(1), in response to the comment that the exchanges should conform their position limits to the federal limits so that a single position limit and accountability regime apply across exchanges,[774] the Commission believes that exchanges may find it prudent in the course of monitoring position limits to impose lower (that is, more restrictive) limit levels. The flexibility for exchanges to set more restrictive limits is granted in CEA section 4a(e), which provides that if an exchange establishes limits on a contract, those limits shall be set at a level no higher than the level of any limits set by the Commission. This expressly permits an exchange to set lower limit levels than federal limit levels. The reproposed rules track this statutory provision.

For purposes of clarification in response to comments on the treatment of basis contracts, the reproposed rules provide a singular definition of ''referenced contract'' which, as stated by the commenters, excludes ''basis contracts.'' For commodities subject to federal limits under reproposed § 150.2, the definition of referenced contract remains the same for federal and exchange-set limits and may not be amended by exchanges. An exchange could, but is not required to, impose limits on any basis contract independently of the federal limit for the commodity in question, but a position in a basis contract with an independent, exchange-set limit would not count for the purposes of the federal limit.[775]

After consideration of comments regarding § 150.5(a)(2)(i) (Grant of exemption),[776] as proposed in the 2016 Supplemental Position Limits Proposal, the Commission is reproposing it with modifications. Reproposed § 150.5(a)(2)(i) provides that any exchange may grant exemptions from any speculative position limits it sets under paragraph § 150.5(a)(1), provided that such exemptions conform to the requirements specified in § 150.3, and provided further that any exemptions to exchange-set limits not conforming to § 150.3 are capped at the level of the applicable federal limit in § 150.2.

The Commission notes that under the 2013 Position Limits Proposal, exchanges could adopt position accountability at a level lower than the federal limit (along with a position limit at the same level as the federal limit); in such cases, the exchange would not need to grant exemptions for positions no greater than the level of the federal limit. Under the Reproposal, exchanges could choose, instead, to adopt a limit lower than the federal limit; in such a case, the Commission would permit the exchange to grant an exemption to the exchange's lower limit, where such exemption does not conform to § 150.3, provided that such exemption to an exchange-set limit is capped at the level of the federal limit. Such a capped exemption would basically have the same effect as if the exchange set its speculative position limit at the level of the federal limit, as required under DCM core principle 5(B) and SEF core principle 6(B)(1).[777]

In regards to the five-day rule, the Commission notes that the reproposed rule does not apply the prudential condition of the five-day rule to non-enumerated hedging positions. The Commission considered the recommendations that the Commission: Allow exchanges to recognize a bona fide hedge exemption for up to a five-day retroactive period in circumstances where market participants need to exceed limits to address a sudden and unforeseen hedging need; specifically authorize exchanges to grant bona fide hedge and spread exemptions during the last five days of trading or less, and/or delegate to the exchanges for their consideration the decision of whether to apply the five-day rule to a particular contract after their evaluation of the particular facts and circumstances. As reproposed, and as discussed in connection with the definition of bona fide hedging position,[778] the five-day rule would only apply to certain positions (pass-through swap offsets, anticipatory and cross-commodity hedges).[779] However, in regards to exchange processes under § 150.9, § 150.10, and § 150.11, the Commission would allow exchanges to waive the five-day rule on a case-by-case basis.

In addition, the Commission proposes to amend § 150.5(a)(2)(ii) (Application for exemption). The reproposed rule would permit exchanges to adopt rules that allow a trader to file an application for an enumerated bona fide hedging exemption within five business days after the trader assumed the position that exceeded a position limit.[780] The Commission expects that exchanges will carefully consider whether allowing such retroactive recognition of an enumerated bona fide hedging exemption would, as noted by one commenter, diminish the overall integrity of the process.[781] In addition, the Commission cautions exchanges to carefully consider whether to adopt in those rules the two safeguards recommended by that commenter: (i) Requiring market participants making use of the retroactive application to demonstrate that the applied-for hedge was required to address a sudden and unforeseen hedging need; and (ii) providing that if the emergency hedge recognition was not granted, exchange rules would continue to require the applicant to unwind its position in an orderly manner and also would deem the applicant to have been in violation for any period in which its position exceeded the applicable limits.[782]

Concerning the comment recommending greater discretion be given DCMs and SEFs that are trading facilities with respect to aggregation requirements, the Commission reiterates its belief in the benefits of requiring exchanges to conform to the federal standards on aggregation, including lower burden and less confusion for traders active on multiple exchanges,[783] efficiencies in administration for both exchanges and the Commission, and the prevention of a ''race-to-the-bottom'' wherein exchanges compete over lower standards. The Commission notes that the provision regarding aggregation in reproposed § 150.5(a)(5) incorporates by reference § 150.4 and thus would, on a continuing basis, reflect any changes made to the aggregation standard provided in the section.

[774] *But see* CL–NGFA–60941 at 2 (urging the Commission to allow exchanges to maintain their current authority to set speculative limits for both spot month and all-months combined limits below federal limits).

[775] The Commission notes that its singular definition of ''referenced contract'' that excludes ''basis contracts'' applies not only to § 150.5(a), but also to § 150.5(b). Separately, the Commission notes that in the future, it may determine to subject basis contracts to a separate class limit in order to discourage potential manipulation of the outright price legs of the basis contract.

[776] *See, e.g.,* CL–ICE–60929 at 2–4, 7–8; CL–Working Group–60947 at 14.

[777] 7 U.S.C. 7(d)(5) and 7 U.S.C. 7b–3(f)(6).

[778] *See* the discussion regarding the five-day rule in connection with the definition of bona fide hedging position in the discussion of § 150.9 (Process for recognition of positions as non-enumerated bona fide hedges).

[779] *See* § 150.1, definition of bona fide hedging position sections (2)(ii)(A), (3)(iii), (4), and (5) (Other enumerated hedging position). To provide greater clarity as to which bona fide hedge positions the five-day rule applies, the reproposed rules reorganize the definition.

[780] The Reproposal includes a similar modification to § 150.5(b)(5)(i).

[781] CL–NCGA–NGSA–60919 at 10–11.

[782] *Id.*

[783] The Commission's belief is supported by requests from multiple traders for industry-wide, standard aggregation requirements.

c. § 150.5(b)—Requirements and Acceptable Practices for Commodity Derivative Contracts That Are Not Subject to Federal Position Limits

i. December 2013 Position Limits Proposal

The Commission set forth in § 150.5(b), as proposed in the December 2013 Position Limits Proposal, requirements and acceptable practices that would generally update and reorganize the set of acceptable practices listed in current § 150.5 as they relate to contracts that are not subject to the federal position limits, including physical and excluded commodities.[784] As discussed above, the Commission also proposed to revise § 150.5 to implement uniform requirements for DCMs and SEFs that are trading facilities relating to hedging exemptions across all types of commodity derivative contracts, including those that are not subject to federal position limits. The Commission further proposed to require DCMs and SEFs that are trading facilities to have uniform aggregation polices that mirrored the federal aggregation provisions for all types of commodity derivative contracts, including for contracts that were not subject to federal position limits.[785]

The previously proposed revisions to DCM and SEF acceptable practices generally concerned how to: (1) Set spot-month position limits; (2) set individual non-spot month and all-months-combined position limits; (3) set position limits for cash-settled contracts that use a referenced contract as a price source; (4) adjust position limit levels after a contract has been listed for trading; and (5) adopt position accountability in lieu of speculative position limits.[786]

For spot months under the December 2013 Position Limits Proposal, for a derivative contract that was based on a commodity with a measurable deliverable supply, previously proposed § 150.5(b)(1)(i)(A) updated the acceptable practice in current § 150.5(b)(1) whereby spot month position limits should be set at a level no greater than one-quarter of the estimated deliverable supply of the underlying commodity.[787] Previously proposed § 150.5(b)(1)(i)(A) clarified that this acceptable practice for setting spot month position limits would apply to any commodity derivative contract, whether physical-delivery or cash-settled, that has a measurable deliverable supply.[788]

For a derivative contract that was based on a commodity without a measurable deliverable supply, the December 2013 Position Limits Proposal proposed for spot months, in § 150.5(b)(1)(i)(B), to codify as guidance that the spot month limit level should be no greater than necessary and appropriate to reduce the potential threat of market manipulation or price distortion of the contract's or the underlying commodity's price.[789]

Under previously proposed § 150.5(b)(1)(ii)(A), the December 2013 Position Limits Proposal preserved the existing acceptable practice in current § 150.5(b)(2) whereby individual non-spot or all-months-combined levels for agricultural commodity derivative contracts that are not subject to the federal limits should be no greater than 1,000 contracts at initial listing. As then proposed, the rule would also codify as guidance that the 1,000 contract limit should be taken into account when the notional quantity per contract is no larger than a typical cash market transaction in the underlying commodity, or reduced if the notional quantity per contract is larger than a typical cash market transaction. Additionally, the December 2013 Position Limits Proposal proposed in § 150.5(b)(1)(ii)(A), to codify for individual non-spot or all-months-combined, that if the commodity derivative contract was substantially the same as a pre-existing DCM or SEF commodity derivative contract, then it would be an acceptable practice for the DCM or SEF that is a trading facility to adopt the same limit as applies to that pre-existing commodity derivative contract.[790]

In § 150.5(b)(1)(ii)(B), the December 2013 Position Limits Proposal preserved the existing acceptable practice for individual non-spot or all-months-combined in exempt and excluded commodity derivative contracts, set forth in current § 150.5(b)(3), for DCMs to set individual non-spot or all-months-combined limits at levels no greater than 5,000 contracts at initial listing.[791] Previously proposed § 150.5(b)(1)(ii)(B) would codify as guidance for exempt and excluded commodity derivative contracts that the 5,000 contract limit should be applicable when the notional quantity per contract was no larger than a typical cash market transaction in the underlying commodity, or should be reduced if the notional quantity per contract was larger than a typical cash market transaction. Additionally, previously proposed § 150.5(b)(1)(ii)(B) would codify a new acceptable practice for a DCM or SEF that is a trading facility to adopt the same limit as applied to the pre-existing contract if the new commodity contract was substantially the same as an existing contract.[792]

The December 2013 Position Limits Proposal provided in § 150.5(b)(1)(iii)

[784] For position limits purposes, § 150.1(k), as proposed in the December 2013 Position Limits Proposal, would define ''physical commodity'' to mean any agricultural commodity, as defined in 17 CFR 1.3, or any exempt commodity, as defined in section 1a(20) of the Act. Excluded commodity is defined in section 1a(19) of the Act.

[785] As Commission noted at that time, hedging exemptions and aggregation policies that vary from exchange to exchange would increase the administrative burden on a trader active on multiple exchanges, as well as increase the administrative burden on the Commission in monitoring and enforcing exchange-set position limits. December 2013 Position Limits Proposal, 78 FR at 75756.

[786] *See* December 2013 Position Limits Proposal, 78 FR at 75757.

[787] As proposed in the December 2013 Position Limits Proposal, § 150.5(b)(1)(i)(A) was consistent with the Commission's longstanding policy regarding the appropriate level of spot-month limits for physical delivery contracts. These position limits would be set at a level no greater than 25 percent of estimated deliverable supply. The spot-month limits would be reviewed at least every 24 months thereafter. The 25 percent formula narrowly targeted the trading that may be most susceptible to, or likely to facilitate, price disruptions. The goal for the formula, as noted in the December 2013 Position Limits Proposal release, was to minimize the potential for corners and squeezes by facilitating the orderly liquidation of positions as the market approaches the end of trading and by restricting swap positions that may be used to influence the price of referenced contracts that are executed centrally. December 2013 Position Limits Proposal, 78 FR at 75756, n. 686.

[788] The Commission noted in the December 2013 Position Limits Proposal that, in general, the term ''deliverable supply'' means the quantity of the commodity meeting a derivative contract's delivery specifications that can reasonably be expected to be readily available to short traders and saleable to long traders at its market value in normal cash marketing channels at the derivative contract's delivery points during the specified delivery period, barring abnormal movement in interstate commerce. Previously proposed § 150.1 would define commodity derivative contract to mean any futures, option, or swap contract in a commodity (other than a security futures product as defined in CEA section 1a(45)). December 2013 Position Limits Proposal, 78 FR at 75756, n. 687.

[789] December 2013 Position Limits Proposal, 78 FR at 75757. The Commission noted that this descriptive standard is largely based on the language of DCM core principle 5 and SEF core principle 6. The Commission does not suggest that an excluded commodity derivative contract that is based on a commodity without a measurable supply should adhere to a numeric formula in setting spot month position limits. *Id.* at 75757, n. 688.

[790] The Commission noted that ''in this context, 'substantially the same' means a close economic substitute. For example, a position in Eurodollar futures can be a close economic substitute for a fixed-for-floating interest rate swap.'' December 2013 Position Limits Proposal, 78 FR at 75757.

[791] In contrast, 17 CFR 150.5(b)(3) lists this as an acceptable practice for contracts for ''energy products and non-tangible commodities.'' Excluded commodity is defined in CEA section 1a(19), and exempt commodity is defined CEA section 1a(20).

[792] December 2013 Position Limits Proposal, 78 FR at 75757.

that if a commodity derivative contract was cash-settled by referencing a daily settlement price of an existing contract listed on a DCM or SEF, then it would be an acceptable practice for a DCM or SEF to adopt the same position limits as the original referenced contract, assuming the contract sizes are the same. Based on its enforcement experience, the Commission expressed the belief that limiting a trader's position in cash-settled contracts in this way would diminish the incentive to exert market power to manipulate the cash-settlement price or index to advantage a trader's position in the cash-settled contract.[793]

In previously proposed § 150.5(b)(2)(i)(A), the Commission was updating the acceptable practices in current § 150.5(c) for adjusting limit levels for the spot month.[794] For a derivative contract that was based on a commodity with a measurable deliverable supply, previously proposed § 150.5(b)(2)(i)(A) maintained the acceptable practice in current § 150.5(c) to adjust spot month position limits to a level no greater than one-quarter of the estimated deliverable supply of the underlying commodity, but would apply this acceptable practice to any commodity derivative contract, whether physical-delivery or cash-settled, that has a measurable deliverable supply. For a derivative contract that was based on a commodity without a measurable deliverable supply, previously proposed § 150.5(b)(2)(i)(B) would codify as guidance that the spot month limit level should not be adjusted to levels greater than necessary and appropriate to reduce the potential threat of market manipulation or price distortion of the contract's or the underlying commodity's price. In addition, the December 2013 Position Limit Proposal would have codified in § 150.5(b)(2)(i)(A) a new acceptable practice that spot month limit levels be reviewed no less than once every two years.[795]

The December 2013 Position Limits Proposal explained that then proposed § 150.5(b)(2)(ii) maintained as an acceptable practice the basic formula set forth in current § 150.5(c)(2) for adjusting non-spot-month limits at levels of no more than 10% of the average combined futures and delta-adjusted option month-end open interest for the most recent calendar year up to 25,000 contracts, with a marginal increase of 2.5% of the remaining open interest thereafter.[796] Previously proposed § 150.5(b)(2)(ii) would also maintain as an alternative acceptable practice the adjustment of non-spot-month limits to levels based on position sizes customarily held by speculative traders in the contract.[797] Previously proposed § 150.5(b)(3) generally updated and reorganized the existing acceptable practices in current § 150.5(e) for a DCM or SEF that is a trading facility to adopt position accountability rules in lieu of position limits, under certain circumstances, for contracts that are not subject to federal position limits. As noted in the December 2013 Position Limits Proposal, this section would reiterate the DCM's authority, with conforming changes for SEFs, to require traders to provide information regarding their position when requested by the exchange.[798] In addition, previously proposed § 150.5(b)(3) would codify a new acceptable practice for a DCM or SEF to require traders to consent to not increase their position in a contract if so ordered, as well as a new acceptable practice for a DCM or SEF to require traders to reduce their position in an orderly manner.[799]

The December 2013 Position Limits Proposal would maintain under § 150.5(b)(3)(i) the acceptable practice for a DCM or SEF to adopt position accountability rules outside the spot month, in lieu of position limits, for an agricultural or exempt commodity derivative contract that: (1) Had an average month-end open interest of 50,000 or more contracts and an average daily volume of 5,000 or more contracts during the most recent calendar year; (2) had a liquid cash market; and (3) was not subject to federal limits in § 150.2—provided, however, that such DCM or SEF that is a trading facility should adopt a spot month speculative position limit with a level no greater than one-quarter of the estimated spot month deliverable supply.[800]

The December 2013 Position Limits Proposal would maintain in § 150.5(b)(3)(ii)(A) the acceptable practice for a DCM or SEF to adopt position accountability rules in the spot month in lieu of position limits for an excluded commodity derivative contract that had a highly liquid cash market and no legal impediment to delivery.[801] For an excluded commodity derivative contract without a measurable deliverable supply, previously proposed § 150.5(b)(3)(ii)(A) would codify an acceptable practice for a DCM or SEF to adopt position accountability rules in the spot month in lieu of position limits because there was not a deliverable supply that was subject to manipulation. However, for an excluded commodity derivative contract that had a measurable deliverable supply, but that may not be highly liquid and/or was subject to some legal impediment to delivery, previously proposed § 150.5(b)(3)(ii)(A) set forth an acceptable practice for a DCM or SEF to adopt a spot-month position limit equal to no more than one-quarter of the estimated deliverable supply for that commodity, because the estimated deliverable supply may be susceptible to manipulation.[802] Furthermore, the December 2013 Position Limits Proposal in § 150.5(b)(3)(ii) would remove the ''minimum open interest and volume'' test for excluded commodity derivative contracts generally.[803] Finally, the December 2013 Position Limits Proposal would codify in § 150.5(b)(3)(ii)(B) an acceptable practice for a DCM or SEF to adopt position accountability levels for an excluded commodity derivative contract in lieu of position limits in the individual non-spot month or all-months-combined.

The December 2013 Position Limits Proposal added in § 150.5(b)(3)(iii) a new acceptable practice for an exchange to list a new contract with position accountability levels in lieu of position limits if that new contract was substantially the same as an existing contract that was currently listed for trading on an exchange that had already

[793] December 2013 Position Limits Proposal, 78 FR at 75757. As the Commission noted with respect to cash-settled contracts where the underlying product is a physical commodity with limited supplies, thus enabling a trader to exert market power (including agricultural and exempt commodities), the Commission has viewed the specification of speculative position limits to be an essential term and condition of such contracts in order to ensure that they are not readily susceptible to manipulation, which is the DCM core principle 3 requirement. *Id.* at 75757, n. 692.

[794] *Id.* at 75757.

[795] *Id.* at 75757–58.

[796] *Id.* at 75758.

[797] *Id.*

[798] *Id. Cf.* 17 CFR 150.5(e)(2)–(3).

[799] December 2013 Position Limits Proposal, 78 FR at 75758.

[800] The December 2013 Position Limits Proposal noted that 17 CFR 150.5(e)(3) applies this acceptable practice to a ''tangible commodity, including, but not limited to metals, energy products, or international soft agricultural products.'' *Id.* at 75758. It also cited to the comparison of the ''minimum open interest and volume test'' in proposed § 150.5(b)(3)(A) to that in current § 150.5(e)(3). *Id.*

[801] *Id.*

[802] *Id.*

[803] *Id.* The December 2013 Position Limits Proposal pointed out that the ''minimum open interest and volume'' test, as presented in 17 CFR 150.5(e)(1)–(2), need not be used to determine whether an excluded commodity derivative contract should be eligible for position accountability rules in lieu of position limits in the spot month. *Id.*

adopted position accountability levels in lieu of position limits.[804]

As previously proposed, § 150.5(b)(4) would maintain the acceptable practice that for contracts not subject to federal position limits, DCMs and SEFs should calculate trading volume and open interest in the manner established in current § 150.5(e)(4).[805] The Commission stated in the December 2013 Position Limits Proposal that then proposed § 150.5(b)(4) would build upon these standards by accounting for swaps in referenced contracts on a futures-equivalent basis.[806]

As noted above, under the December 2013 Position Limits proposal, the Commission proposed to require DCMs and SEFs to have uniform hedging exemptions and aggregation polices that mirror the federal aggregation provisions for all types of commodity derivative contracts, including for contracts that are not subject to federal position limits. The Commission explained that hedging exemptions and aggregation policies that vary from exchange to exchange would increase the administrative burden on a trader active on multiple exchanges, as well as increase the administrative burden on the Commission in monitoring and enforcing exchange-set position limits.[807] Therefore, the December 2013 Position Limits Proposal in § 150.5(b)(5)(i) would require any hedge exemption rules adopted by a designated contract market or a swap execution facility that is a trading facility to conform to the definition of bona fide hedging position in previously proposed § 150.1.[808]

The December 2013 Position Limits Proposal also set forth in § 150.5(b)(5)(ii) acceptable practices for DCMs and SEFs to grant exemptions from position limits for positions, other than bona fide hedging positions, in contracts not subject to federal limits. The exemptions in § 150.5(b)(5)(ii) under the December 2013 Position Limits Proposal generally tracked the exemptions then proposed in § 150.3; acceptable practices were suggested based on the same logic that underpinned those exemptions.[809] The acceptable practices contemplated that a DCM or SEF might grant exemptions under certain circumstances for financial distress, intramarket and intermarket spread positions (discussed above), and qualifying cash-settled contract positions in the spot month.[810] Previously proposed § 150.5(b)(5)(ii)(E) also set forth an acceptable practice for a DCM or SEF to grant for contracts on excluded commodities, a limited risk management exemption pursuant to rules submitted to the Commission, and consistent with the guidance in new Appendix A to part 150.[811]

The December 2013 Position Limits Proposal provided in § 150.5(b)(6)–(7) acceptable practices relating to pre-enactment and transition period swap positions (as those terms were defined in previously proposed § 150.1),[812] as well as to commodity derivative contract positions acquired in good faith prior to the effective date of mandatory federal speculative position limits.[813]

Additionally, for any contract that is not subject to federal position limits, previously proposed § 150.5(b)(8) required the DCM or SEF that is a trading facility to conform to the uniform federal aggregation provisions.[814] As noted above, aggregation policies that vary from exchange to exchange would increase the administrative burden on a trader active on multiple exchanges, as well as increase the administrative burden on the Commission in monitoring and enforcing exchange-set position limits. The requirement generally mirrored the requirement in § 150.5(a)(5) for contracts that are subject to federal position limits by requiring the DCM or SEF that is a trading facility to have aggregation rules that conform to previously proposed § 150.4.[815]

ii. Comments Received to December 2013 Position Limits Proposal Regarding § 150.5(b)

Three commenters on previously proposed regulation § 150.5 recommended that the Commission not require SEFs to establish position limits.[816] Two noted that because SEF participants may use more than one derivatives clearing organization (''DCO''), a SEF may not know when a position has been offset.[817] Further, during the ongoing SEF registration process,[818] a number of entities applying to become registered as SEFs told the Commission that they lacked access to information that would enable them to knowledgeably establish position limits or monitor positions.[819] The Commission observes that this

[804] *See supra* discussion of what is meant by ''substantially the same'' in this context. *See also* December 2013 Position Limits Proposal, 78 FR at 75757, n. 690.

[805] As noted in the December 2013 Position Limits Proposal, for SEFs, trading volume and open interest for swaptions should be calculated on a delta-adjusted basis. *See id.* at 75758, n. 697.

[806] *See id.* at 75698–99 (defining ''Futures-equivalent'' in § 150.1 to account for swaps in referenced contracts).

[807] *See* December 2013 Position Limits Proposal, 78 FR at 75756. *See also supra* regarding § 150.5(a)(5).

[808] The requirement proposed in § 150.5(b)(8) that DCMs and SEFs have uniform aggregation polices that mirror the federal aggregation provisions is addressed below.

[809] *See* December 2013 Position Limits Proposal, 78 FR at 75735–41, 75827–28. *See also supra* discussion of the § 150.3 exemptions.

[810] *See id.*

[811] As the Commission noted, previously proposed Appendix A to part 150 ''is intended to capture the essence of the Commission's 1987 interpretation of its definition of bona fide hedge transactions to permit exchanges to grant hedge exemptions for various risk management transactions. *See* Risk Management Exemptions From Speculative Position Limits Approved Under Commission Regulation 1.61, 52 FR 34633, Sep. 14, 1987.'' The Commission also specified that such exemptions be granted on a case-by-case basis, subject to a demonstrated need for the exemption, required that applicants for these exemptions be typically engaged in the buying, selling, or holding of cash market instruments, and required the exchanges to monitor the exemptions they granted to ensure that any positions held under the exemption did not result in any large positions that could disrupt the market. *Id. See also* December 2013 Position Limits Proposal, 78 FR at 75756, n. 683.

[812] *See supra* discussion of pre-enactment and transition period swap positions.

[813] December 2013 Position Limits Proposal, 78 FR at 75756, 75831.

[814] Proposed § 150.5(b)(7) would replace 17 CFR 150.5(g) as it relates to contracts that are not subject to federal position limits.

[815] *Id.* at 75756.

[816] CL–CMC–59634 at 14–15; CL–FIA–60392 at 10; and CL–ISDA/SIFMA–59611 at 35. One commenter stated that SEFs should be exempt from the requirement to set positions limits because SEFs are in the early stages of development and could be harmed by limits that restrict liquidity. CL–ISDA/SIFMA–59611 at 35.

[817] CL–CMC–59634 at 14–15; and CL–FIA–60392 at 10.

[818] Under CEA section 5h(a)(1), no person may operate a facility for trading swaps unless the facility is registered as a SEF or DCM. 7 U.S.C. 7b–3(a)(1). A SEF must comply with core principles, including Core Principle 6 regarding position limits, as a condition of registration. CEA section 5h(f)(1), 7 U.S.C. 7b–3(f)(1).

[819] For example, in a submission to the Commission under part 40 of the Commission's regulations, BGC Derivative Markets, L.P. states that ''[t]he information to administer limits or accountability levels cannot be readily ascertained. Position limits or accountability levels apply market-wide to a trader's overall position in a given swap. To monitor this position, a SEF must have access to information about a trader's overall position. However, a SEF only has information about swap transactions that take place on its own Facility and has no way of knowing whether a particular trade on its facility adds to or reduces a trader's position. And because swaps may trade on a number of facilities or, in many cases, over-the-counter, a SEF does not know the size of the trader's overall swap position and thus cannot ascertain whether the trader's position relative to any position limit. Such information would be required to be supplied to a SEF from a variety of independent sources, including SDRs, DCOs, and market participants themselves. Unless coordinated by the Commission operating a centralized reporting system, such a data collection requirement would be duplicative as each separate SEF required reporting by each information sources.'' BGC Derivative Markets, L.P., Rule Submission 2015–09 (Oct. 6, 2015).

information gap would also be a concern for DCMs in respect of swaps.

One commenter expressed the view that deliverable supply calculations used to establish spot month limits should be based on commodity specific actual physical transport/transmission, generation and production.[820]

One commenter urged the Commission to allow the listing exchange to set non-spot month limits at least as high as the spot-month position limit, rather than base the non-spot month limit strictly on the open interest formula.[821] Another commenter recommended that the Commission remove from § 150.5(b)(1)(ii)(B) the provision setting a 5,000 contract limit for non-spot-month or all-months-combined accountability levels for exempt commodities, because that level may not be appropriate for all markets; instead, the Commission should rely on the exchanges to set accountability levels for exempt commodity markets.[822]

One commenter recommended that DCMs be permitted to establish position accountability levels in lieu of position limits outside of the spot month.[823] The commenter recommended that the administration of position accountability should be coordinated with the Commission and other DCMs to the extent that a market participant holds positions on more than one DCM.[824]

iii. 2016 Supplemental Position Limits Proposal

In the 2016 Supplemental Position Limits Proposal, the Commission proposed to revise § 150.5(b)(5) from what was proposed in the December 2013 Position Limits Proposal; proposed § 150.5(b) establishes requirements and acceptable practices that pertain to commodity derivative contracts not subject to federal position limits.[825] The proposed revisions to § 150.5(b)(5) would, under the 2016 Supplemental Position Limits Proposal, permit exchanges, in regards to commodity derivative contracts not subject to federal position limits, to recognize non-enumerated bona fide hedging positions, as well as spreads. Moreover, the exchanges would no longer be prohibited from recognizing spreads during the spot month.[826] Instead, as the Commission noted in the 2016 Supplemental Position Limits Proposal, what it was proposing would, in part, maintain the status quo: Exchanges that currently recognize spreads in the spot month under current § 150.5(a) would be able to continue to do so. Rather than a prohibition, the exchanges would be responsible for determining whether recognizing spreads, including spreads in the spot month, would further the policy objectives in section 4a(a)(3) of the Act.[827]

iv. Comments Received to 2016 Supplemental Position Limits Proposal Regarding § 150.5(b)

Exchange-Administered Exemptions Under § 150.5(b)

Several commenters requested clarification as to the application of exchange-administered exemption requests to non-referenced contracts generally under § 150.5(b).[828] In addition, several commenters raised concerns with the requirement in § 150.5(b)(5)(i) that the exchanges provide exemptions ''in a manner consistent with the process described in § 150.9(a).'' [829] Similarly, according to one commenter, the exchanges should not be bound to the same exemption process provided under proposed CFTC Regulation 150.9 when administering exemptions from exchange-set limits. Rather, the commenter recommended that the Commission: ''(i) not adopt proposed CFTC Regulation 150.5(b)(5)(i) in any final rule issued in this proceeding or (ii) clarify that the phrase 'in a manner consistent with the process described in [proposed CFTC Regulation] 150.5(b)(5)(i)' does not mean that the Exchanges must apply the virtually identical process for recognizing non-enumerated bona fide hedging positions under proposed CFTC Regulation 150.9(a) to their exemption process for exchange-set speculative position limits.'' [830]

Another commenter stated that the Commission should remove the requirements of § 150.5(b) that apply the exemption procedures of § 150.9 to exemptions granted for contracts in excluded commodities and physical commodities that are not subject to federal position limits. In support of this request, the commenter maintained that exchange exemption programs have been operating successfully without the need for such rules, and exchanges do not require additional guidance from the Commission on how to assess recognitions under the 2016 Supplemental Position Limits Proposal and that rule enforcement reviews are adequate.[831]

Treatment of Spread and Anticipatory Hedge Exemptions Under § 150.5(b)

Several commenters requested that the Commission clarify that spread and anticipatory hedge exemptions are unnecessary for excluded commodities and other products not subject to federal limits. For example, one commenter seeks clarity regarding the application of § 150.5(b) to spread exemption and anticipatory hedge exemption requests, stating that ''[p]roposed section 150.5(b) is silent with respect to anticipatory hedges contemplated under the process in proposed section 150.11, and makes no reference in proposed section 150.5(b)(5)(ii)(C) to the process in proposed section 150.10 when describing spread exemptions an exchange may recognize. The Commission must clarify whether it intends that market participants and exchanges may avail themselves of such processes in applying for and recognizing exemptions from exchange limits for non-referenced contracts.'' [832] On the other hand, in the associated footnote, the same commenter observes ''[h]owever, in its cost-benefit analysis, the Commission notes that proposed section 150.11 'works in concert with' 'proposed § 150.5(b)(5), with the effect that recognized anticipatory enumerated

[820] CL–EDF–60398 at 6–7.

[821] CL–ICE–59962 at 7.

[822] CL–Nodal–59695 at 3.

[823] CL–FIA–59595 at 5, 39 and 41; *see also* CL–FIA–60303 at 3–4.

[824] CL–FIA–60392 at 9.

[825] 2016 Supplemental Position Limits Proposal, 81 FR at 38482.

[826] *Id.* at 38482, 38506–7. *Compare* December 2013 Position Limits Proposal, 78 FR at 75830.

[827] 2016 Supplemental Position Limits Proposal, 81 FR at 38482, 38506–07.

[828] CMC, for example, requested that the Commission clarify that exchange-granted hedge exemption procedures would be ''applicable if, and to the extent that, the exchange granted exemption exceeds federally established speculative position limits and not otherwise.'' CL–CMC–60950 at 14. According to CME, on the other hand, proposed section 150.5(b) was unclear and ambiguous and so should be reproposed. For example, CME stated that the proposal was ''riddled with ambiguities and potential oversights,'' and, in connection with non-referenced contracts under section 150.5(b), CME also stated ''the scope of exchange discretion under proposed section 150.9(a) is unclear. Thus, exchanges could be bound by the five-day rule in recognizing as NEBFH positions certain enumerated hedge strategies for non-referenced contracts, despite the same five-day rule limitation not applying in similar scenarios today.'' CL–CME–60926 at 14–15.

[829] CL–CME–60926 at 14–15; CL–Working Group–60947 at 14; and CL–ICE–60929 at 8. For example, CME stated that requiring exchanges to recognize non-enumerated bona fide hedge positions for non-referenced contracts ''in a manner consistent with the process described in § 150.9(a)'' appears to ''break with historical practice in administering NEBFHs for non-referenced contracts,'' and ''would appear to impose new burdensome and unnecessary compliance obligations on market participants that do not exist today.'' CL–CME–60926 at 14–15.

[830] CL–Working Group–60947 at 14.

[831] CL–ICE–60929 at 8.

[832] CL–CME–60926 at 15.

bona fide hedging positions may exceed exchange-set position limits for contracts not subject to federal position limits.' '' [833]

Another commenter urges the Commission to clarify that spread and anticipatory hedge exemptions are unnecessary for excluded commodities and other products not subject to federal limits. In this regard, the commenter seeks the removal of requirements found in § 150.5(b).[834] A third commenter states that extending the requirements for exchange hedge exemption rules to contracts on excluded commodities is ''clearly an error'' that needs to be rectified, stating that there was no discussion of this expansion in the preamble to the Supplemental. According to the commenter, ''there is no basis in the Dodd-Frank amendments to the CEA for this extension of the Commission's authority over exchange position limits on excluded commodities. To the contrary, that authority is clearly limited to position limits on contracts on physical commodities.'' [835]

Reporting Requirements Under § 150.5(b)

According to one commenter, the 2016 Supplemental Position Limits Proposal does not provide any explanation regarding the Commission's need to receive from the exchanges the same exemption reports for non-referenced contracts that it would receive for referenced contracts. The commenter states that the 2016 Supplemental Position Limits Proposal characterizes exchange submissions of exemption recipient reports to the CFTC as ''support[ing] the Commission's surveillance program, by facilitating the tracking of non-enumerated bona fide hedging positions recognized by the exchange, and helping the Commission to ensure that an applicant's activities conform to the terms of recognition that the exchange has established.'' [836] While acknowledging that the Commission has a surveillance obligation with respect to federal limits, the commenter maintains that, ''the same obligation has never before existed with respect to exchange-set limits for non-referenced contracts, and does not exist today.'' [837] The commenter also states that the Commission has misinterpreted its mandate and therefore should drop this unnecessary reporting requirement and related procedures with respect to non-referenced contracts.''

Five-Day Rule Under § 150.5(b)

As noted above, several commenters [838] addressed the five-day rule, suggesting that the decision whether to apply the five-day rule to a particular contract should be delegated to the exchanges as the exchanges are in the best position to evaluate facts and circumstances, and different markets have different dynamics and needs.[839] And, specifically in connection with non-referenced contracts under § 150.5(b), one commenter states that, as it believes that the scope of exchange discretion under proposed section 150.9(a) is unclear, ''exchanges could be bound by the five-day rule in recognizing as non-enumerated bona fide hedging positions certain enumerated hedge strategies for non-referenced contracts, despite the same five-day rule limitation not applying in similar scenarios today.'' [840]

Comment Letter Received After the Close of the Comment Period for the 2016 Supplemental Position Limits Proposal Regarding Limit Levels Under § 150.5(b)

One commenter noted that when the CEA addresses ''linked contracts'' in CEA section 4(b)(1)(B)(ii)(I), in relation to FBOTS, it provides that the Commission may not permit an FBOT to provide direct access to participants located in the United States unless the Commission determines that the FBOT (or the foreign authority overseeing the FBOT) adopts position limits that are comparable to the position limits adopted by the registered entity for the contract(s) against which the FBOT contract settles.[841] According to the commenter, CEA section 4(b), which was added by the Dodd-Frank Act, ''contains an explicit Congressional endorsement of 'comparable' '' limits for cash-settled contracts in relation to the physically-delivered contracts to which they are linked.[842] The statutory definition of ''linked contract,'' the commenter stated, ''mirrors the definition of 'referenced contract' in the Commission's 2013 position limits proposal: Both definitions capture cash-settled contracts that are 'linked' to the price of a physically-delivered contract traded on a DCM (referred to as a 'core referenced futures contract' in the proposal).'' [843] That commenter stated that the only place in the CEA which addresses how to treat a cash-settled contract and its physically-delivered benchmark contract for position limit purposes is in CEA section 4(b), claiming that ''Congress unmistakably wanted the two trading instruments to be treated 'comparably.' '' [844]

In addition, according to the commenter, when the Commission, in response to the Dodd-Frank Act provisions regarding FBOTs in amended CEA section 4(b), adopted final § 48.8(c)(1)(ii)(A), ''it acknowledged that a linked contract and its physically-delivered benchmark contract 'create a single market' capable of being affected through trading in either of the linked or physically-delivered markets,'' and further noted that the Commission ''observed that the price discovery process would be protected by 'ensuring that [ ] linked contracts have position limits and accountability provisions that are comparable to the corresponding [DCM] contracts [to which they are linked].' '' [845]

iv. Commission Determination Regarding § 150.5(b)

The Commission has determined to repropose *§ 150.5(b) generally* as proposed in the the 2016 Supplemental Position Limits Proposal, for the reasons stated above, with specific exceptions discussed below.[846] An overall non-substantive change has been made in reproposing § 150.5 pertaining to excluded commodities. To provide

[833] *Id.*

[834] CL–CMC–60950 at 14.

[835] CL–ISDA–60931 at 11.

[836] CL–CME–60926 at 15, quoting the 2016 Supplemental Position Limits Proposal, 81 FR at 38475.

[837] *Id.*

[838] *E.g.,* CL–NCGA–ASA–60917 at 1–2; CL–CME–60926 at 14–15; CL–ICE–60929 at 7–8; CL–ISDA–60931 at 11; CL–CCI–60935 at 3; CL–MGEX–60936 at 4; CL–Working Group–60947 at 5, 7–9; CL–IECAssn–60949 at 7–9; CL–CMC–60950 at 9–14; CL–NCC–ACSA–60972 at 2.

[839] *See, e.g,* CL–ISDA–60931 at 10; CL–CCI–60935 at 3; CL–MGEX–60936 at 11; CL–Working Group–60947 at 7–9.

[840] CL–CME–60926 at 14–15.

[841] *See* CL–CME–61007 at 2–4; CL–CME–61008 at 2–3.

[842] *See* CL–CME–61007 at 2.

[843] *Id.* at 3. CME claims that the underlying Congressional intent is clear, stating that whether a cash-settled contract is called a ''linked contract'' or a ''referenced contract,'' ''the limit levels and hedge exemptions for that contract and the related physically-delivered contract must be 'comparable.'' *Id.*

[844] *Id.*

[845] *Id.* [footnotes omitted]. The Commission notes that CME incorrectly attributed preamble language as pertaining to § 48.8(c)(1)(ii)(A), which addresses statutory requirements, when it stated that the Commission ''acknowledged that a linked contract and its physically-delivered benchmark contract 'create a single market' capable of being affected through trading in either of the linked or physically-delivered markets'' as this discussion actually addressed the Commission's adoption of its second set of conditions for linked contracts, found in § 48.8(c)(2) (Other Conditions on Linked Contracts).

[846] The Commission is reproposing the following sections without further discussion, for the reasons provided above, since no substantive comments were received: § 150.5(b)(6)(Pre-enactment and transition period swap positions), § 150.5(b)(7) (Pre-existing positions), and § 150.5(b)(9) (Additional acceptable practices).

greater clarity regarding which provisions concern excluded commodities, the Commission proposes to move all provisions applying to excluded commodities from § 150.5(b) into § 150.5(c). As the Commission observed in the December 2013 Position Limits Proposal, ''CEA section 4a(a) only mandates position limits with respect to physical commodity derivatives (*i.e.,* agricultural commodities and exempt commodities).

Additionally, the Commission proposes to make some substantive revisions specific to excluded commodities in what was previously § 150.5 (b), addressed in the discussion of § 150.5(c).

Limit Levels for Commodity Derivative Contracts in a Physical Commodity Not Subject to Federal Limits

In response to the comment regarding the method for calculating deliverable supply, the Commission notes that guidance for calculating deliverable supply can be found in Appendix C to part 38. Amendments to part 38 are beyond the scope of this rulemaking. However, that guidance already provides that deliverable supply calculations are estimates based on what ''reasonably can be expected to be readily available'' on a monthly basis based on a number of types of data from the physical marketing channels, as suggested by the commenter, and these calculations are done for each month and each commodity separately. Furthermore, much of § 150.5(b) reiterates longstanding guidance and acceptable practices for DCMs, rather than proposing new concepts for administering limits on contracts that are not subject to federal limits under § 150.2.

The Commission agrees with the commenter urging the Commission to allow exchanges to set non-spot month limits at least as high as the spot-month position limit, in the event the open interest formula would result in a limit level lower than the spot month. Accordingly, consistent with the recommended revisions to the initial limit level listings for contracts subject to federal limits found in § 150.2(e)(4)(iv), the Commission proposes to revise § 150.5(b)(2)(ii) to allow exchanges to set non-spot month limit levels at the maximum of the spot month limit level, the level derived from the 10/2.5% formula, or 5,000 contracts. To conform with those revisions, the Commission also proposes to revise § 150.5(b)(1)(ii)(A)–(B) to remove the distinction between agricultural and exempt commodities.

Regarding the commenter who expressed concern regarding requirements for accountability levels for exempt commodities, the Commission notes that the provisions set forth guidance and acceptable practices for exchanges in setting position limit levels and accountability levels and, as guidance and acceptable practices, are not binding regulations. Under the Commission's guidance, an initial non-spot month limit level of no more than 5,000 is viewed as suitable.

Similarly, in response to the commenter who recommended that DCMs be permitted to establish position accountability levels in lieu of position limits outside the spot month and coordinate the administration of such levels with the Commission and other DCMs, the Commission agrees that position accountability may be permitted for certain physical commodity derivative contracts. Reproposed § 150.5(b)(3), therefore, provides guidance and acceptable practices concerning exchange adoption of position accountability outside the spot month for contracts having an average month-end open interest of 50,000 contracts and an average daily volume of 5,000 or more contracts during the most recent calendar year and a liquid cash market. The Commission again notes that guidance and acceptable practices do not establish mandatory means of compliance. As such, in regards to meeting the specified volume and open interest thresholds in § 150.5(b)(3), the Commission notes that the guidance in § 150.5(b)(3)(i) may not be the only circumstances under which sufficiently high liquidity may be shown to exist for the establishment of position accountability levels in lieu of position limits.

The December 2013 Position Limits Proposal provided in § 150.5(b)(1)(iii) that if a commodity derivative contract was cash-settled by referencing a daily settlement price of an existing contract listed on a DCM or SEF, then it would be an acceptable practice for a DCM or SEF to adopt the same position limits as the original referenced contract, assuming the contract sizes are the same.[847] However, the Commission is reproposing § 150.5(b)(1)(iii) with a modification: While the previously proposed guidance in § 150.5(b)(1)(iii) provided that the exchange should adopt the ''same'' spot-month, individual non-spot month, and all-months combined limit levels as the original price referenced contract, the Commission is reproposing § 150.5(c)(1)(iii) to provide that the limit levels should, instead, be ''comparable.''

As pointed out by one commenter,[848] the CEA establishes a comparability standard for linked FBOT contracts in CEA section 4(b)(1)(B)(ii)(I), when it provides that the Commission may not permit an FBOT to provide direct access to participants located in the United States unless the Commission determines that the FBOT (or the foreign authority overseeing the FBOT) adopts position limits that are ''comparable to'' the position limits adopted by the registered entity for the contract(s) against which the FBOT contract settles.[849] In addition, as noted by the commenter, the Commission, in adopting § 48.8(c)(2), recognized that the comparability standard and its associated requirements would protect the price discovery process by ensuring that the linked contracts and the U.S. contracts to which they are linked ''have position limits and accountability provisions that are comparable to the corresponding [DCM] contracts [to which they are linked].' '' [850] The Commission notes that this change will better align § 150.5(b)(1)(iii) with the statute and with the standard provided in § 48.8(c).[851] Moreover, use of

[847] The Commission expressed the belief that, based on its enforcement experience, limiting a trader's position in cash-settled contracts in this way would diminish the incentive to exert market power to manipulate the cash-settlement price or index to advantage a trader's position in the cash-settled contract. *See* December 2013 Position Limits Proposal, 78 FR at 75757. As the Commission noted with respect to cash-settled contracts where the underlying product is a physical commodity with limited supplies, thus enabling a trader to exert market power (including agricultural and exempt commodities), the Commission has viewed the specification of speculative position limits to be an essential term and condition of such contracts in order to ensure that they are not readily susceptible to manipulation, which is the DCM core principle 3 requirement. *Id.* at 75757, n. 692.

[848] *See, e.g.,* CL–CME–61007 at 2–4; CL–CME–61008 at 2–3.

[849] CL–CME–61007 at 2. ''Registered entities'' are defined in CEA section 1a(40) as DCMs, DCOs, SEFs, SDRs, notice-registered DCMs under CEA section 5f, and any electronic trading facility upon which a contract is executed or traded which the Commission has determined is a significant price discovery contract. According to CME, CEA Section 4(b) ''contains an explicit Congressional endorsement of 'comparable' '' limits for cash-settled contracts in relation to the physically-delivered contracts to which they are linked. *See* CL–CME–61007 at 2.

[850] CL–CME–61007 at 3. *See* 76 FR 80674, 80685, 80697 (Dec. 23, 2011). *See also* § 48.8(c)(1)(ii)(A).

[851] The comparability standard is also used in determinations as to which foreign DCOs are subject to comparable, comprehensive supervision and regulation by the appropriate government authority in the DCO's home country. See CEA section 5b)(h). *See also* the Commission's Notice of Comparability Determination for Certain Requirements Under the European Market Infrastructure Regulation, 81 FR 15260 (Mar. 22, 2016).

''comparable'' rather than ''same'' limit levels provides exchanges with a more flexible standard based on statutory language.[852] This change also provides a standard that is consistent with existing practice for domestic contracts that are linked to the price of a physical-delivery contract.[853]

The Commission proposes to revise § 150.5(b)(4)(B) regarding the calculation of open interest for use in setting exchange-set speculative position limits to provide that a DCM or SEF that is a trading facility would include swaps in their open interest calculation only if such entities are required to administer position limits on swap contracts of their facilities. This revision clarifies and harmonizes § 150.5(b)(4)(B) with the relief in Appendix E to part 150, as well as in appendices to parts 37 and 38, which delays for DCMs and SEFs that are trading facilities and lack access to sufficient swap position information the requirement to establish and monitor position limits on swaps at this time. This approach conforms § 150.5(b) with other proposed changes regarding the treatment of swaps.[854]

Exchange—Administered Exemptions for Commodity Derivative Contracts in a Physical Commodity Not Subject to Federal Limits

The Commission is reproposing § 150.5(b)(5)(i) with modifications to clarify that it is guidance rather than a regulatory requirement. In addition, as modified, it provides that under exchange rules allowing a trader to file an application for an enumerated bona fide hedging exemption, the application should be filed no later than five business days after the trader assumed the position that exceeded a position limit.[855] As noted above, the Commission expects that exchanges will carefully consider whether allowing retroactive recognition of an enumerated bona fide hedging exemption would, as noted by one commenter, diminish the overall integrity of the process, and should carefully consider whether to adopt in those rules the two safeguards noted: (i) To continue to require market participants making use of the retroactive application to demonstrate that the applied-for hedge was required to address a sudden and unforeseen hedging need; and (ii) providing that if the emergency hedge recognition was not granted, exchange rules would continue to require the applicant to promptly unwind its position and also would deem the applicant to have been in violation for any period in which its position exceeded the applicable limits.

Additionally, the Commission is reproposing § 150.5(b)(5)(i) with modifications to clarify, as requested by commenters,[856] that the exchanges have reasonable discretion as to whether they apply to their exemption process from exchange-set speculative position limits, a virtually identical process as provided for recognizing non-enumerated bona fide hedging positions under CFTC Regulation 150.9(a). As explained in the discussion regarding the changes to the bona fide hedging definition under § 150.1, the Commission is proposes a phased approach with respect to the definition of a bona fide hedging position applicable to physical commodities.[857] The Commission recognizes that exchanges, under § 150.9, may need to adapt their current process to recognize non-enumerated bona fide hedging positions for commodity derivative contracts that are subject to a federal position limit under § 150.2, or adopt a new one. In turn, market participants will need to seek recognition of a non-enumerated bona fide hedge from an exchange under that new process. In light of this implementation issue, the Commission proposes to limit the mandatory scope of the new definition of bona fide hedging position to contracts that are subject to a federal position limit.[858] This means that the Commission would permit exchanges to maintain both their current bona fide hedging position definition and their existing processes for recognizing non-enumerated bona fide hedging positions for physical commodity contracts not subject to federal limits under § 150.2. The Commission notes an exchange may, but need not, adopt for physical commodities not subject to federal limits the new bona fide hedging position definition and the new process to recognize non-enumerated bona fide hedging positions.

In addition, the Commission is proposing that, for enumerated bona fide hedging positions, exchange rules may allow traders to file an application for an enumerated bona fide hedging exemption within five business days after the trader assumed the position that exceeded a position limit.

Finally, as to § 150.5(b)(5)(ii) (Other exemptions), the Commission did not receive any comments regarding § 150.5(b)(5)(ii)(A) (Financial distress), and is reproposing this exemption without change.

Conditional Spot Month Limit Exemption for Commodity Derivative Contracts in a Physical Commodity Not Subject to Federal Limits

While the conditional spot month limit exemption is addressed in more detail under § 150.3, after consideration of comments, the Commission is reproposing § 150.5(b)(5)(ii)(B) with a modification.[859] The December 2013

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[852] As the Commission explained in preamble to final part 48 in connection with comparability determinations, ''[t]he Commission's determination of the comparability of the foreign regulatory regime to which the FBOT applying for registration is subject will not be a ''line by line'' examination of the foreign regulator's approach to supervision of the FBOTs it regulates. Rather, it will be a principles-based review conducted in a manner consistent with the part 48 regulations pursuant to which the Commission will look to determine if that regime supports and enforces regulatory objectives in the oversight of the FBOT and the clearing organization that are substantially equivalent to the regulatory objectives supported and enforced by the Commission in its oversight of DCMs and DCOs.'' 76 FR 80674, 80680 (Dec. 23, 2011). *See also* § 48.5(d)(5).

[853] For example, both CME and ICE currently have conditional spot-month limit exemptions for cash-settled natural gas contracts at a level up to five times the level of the spot-month limit level on CME's economically-equivalent NYMEX Henry Hub Natural Gas (physical-delivery) futures contract to which they settle.

[854] As noted above, the relief was proposed in the 2016 Supplemental Position Limits Proposal, 81 FR at 38459–62. *See also* DCM Core Principle 5, Position Limitations or Accountability (contained in CEA section 5(d)(5), 7 U.S.C. 7(d)(5)) and SEF Core Principle 6, Position Limits or Accountability (contained in CEA section 5h(f)(6), 7 U.S.C. 7b–3(f)(6)).

[855] The modification made to § 150.5(b)(5)(i) is similar manner to its the Commission's modification of § 150.5(a)(2)(ii), but, as mentioned, § 150.5(b)(5)(i) is guidance rather than a regulatory requirement.

[856] *See* CL-Working Group-60947 at 14; *see also* CL–ICE–60929 at 8, 32. As previously proposed, § 150.5(b)(5)(i) provides, ''(i) Hedge exemption. Any hedge exemption rules adopted by a designated contract market or swap execution facility that is a trading facility must conform to the definition of bona fide hedging position in § 150.1 or provide for recognition as a non-enumerated bona fide hedge in a manner consistent with the process described in § 150.9(a).''

[857] *See also* December 2013 Position Limits Proposal, 78 FR at 75725 (stating ''[t]he Commission is proposing a phased approach to implement the statutory mandate. The Commission is proposing in this release to establish speculative position limits on 28 core referenced futures contracts in physical commodities. The Commission anticipates that it will, in subsequent releases, propose to expand the list of core referenced futures contracts in physical commodities. The Commission believes that a phased approach will (i) reduce the potential administrative burden by not immediately imposing position limits on all commodity derivative contracts in physical commodities at once, and (ii) facilitate adoption of monitoring policies, procedures and systems by persons not currently subject to positions limits (such as traders in swaps that are not significant price discovery contracts.). . . . Thus, in the first phase, the Commission generally is proposing limits on those contracts that it believes are likely to play a larger role in interstate commerce than that played by other physical commodity derivative contracts.'').

[858] *See also supra* discussion under regarding the bona fide hedging position definition.

[859] Most comments concerning the conditional spot month limit were submitted by CME and ICE;

Position Limits Proposal proposed guidance that an exchange may adopt a conditional spot month position limit exemption for cash-settled contracts, with one of two provisos being that such positions should not exceed five times the level of the spot-month limit specified by the exchange that lists the physical-delivery contract to which the cash-settled contracts were directly or indirectly linked.[860] As reproposed, the guidance recommends that such conditional exemptions should not exceed two times the level of the spot-month limit specified by the exchange that lists the applicable physical-delivery contract.

After review of comments and an impact analysis regarding the federal limits, the Commission believes that a five-times conditional exemption is too large, other than in natural gas because, in the markets that the Commission proposes to subject to federal limits, the Commission observed few or no market participants with positions in cash-settled contracts in the aggregate that exceed 25 percent of deliverable supply in the spot month. This is so even though cash-settled contracts that are swaps are not currently subject to position limits. A five-times conditional exemption would not ensure liquidity for bona fide hedgers in the spot month for cash-settled contracts because there appear to be few or no positions that large (other than in natural gas). Consequently, and in light of the other three policy objectives of CEA section 4a(a)(3)(B), the Commission reproposes a more cautious approach.[861]

Since transactions of large speculative traders may tend to cause unwarranted price changes, exchanges should exercise caution in determining whether such conditional exemptions are warranted; for example, an exchange may determine that a conditional exemption is warranted because such a speculative trader is demonstrably providing liquidity for bona fide hedgers. Where an exchange may not have access to data regarding a market participant's cash-settled positions away from a particular exchange, such exchange should require, for any conditional spot-month limit exemption it grants, that a trader report promptly to such exchange the trader's aggregate positions in cash-settled contracts, physical-delivery contracts, and cash market positions.

As noted above, under reproposed § 150.5(b)(5)(ii)(B), an exchange has the choice of whether or not to adopt a conditional spot month position limit exemption for cash-settled contracts that are not subject to federal limits. As also discussed above regarding reproposed § 150.3(c), the Commission is not proposing a conditional spot-month limit for agricultural contracts subject to federal limits under reproposed § 150.2. Further, the Commission notes that the current cash-settled natural gas spot month limit rules of two commenters, CME Group (which operates NYMEX) and ICE, both include the same spot-month limit level and the same conditional spot-month limit exemption. In each case the current cash-settled conditional exemption is five times the limit for the physical-delivery contract. Such natural gas contracts would be subject to federal limits under reproposed § 150.2, so the guidance in reproposed § 150.5(b) would not be applicable to those contracts.[862]

Treatment of Spread and Anticipatory Hedge Exemptions for Commodity Derivative Contracts in a Physical Commodity Not Subject to Federal Limits

In regards to the exemption for intramarket and intermarket spread positions under § 150.5(b)(5)(ii)(C), the comments received concerned the exchange process for providing spread exemptions under § 150.10. The Commission addresses those comments below in its discussion of § 150.10, and is reproposing § 150.5(b)(5)(ii)(C) as proposed in the 2016 Supplemental Position Limits Proposal.

The Commission points out, however, that reproposed § 150.5(b)(5)(ii)(C) would apply only to physical commodity derivative contracts, and would not apply to any derivative contract in an excluded commodity. Furthermore, as noted above, reproposed § 150.5(b)(5)(ii)(C) provides guidance rather than rigid requirements. Instead, under § 150.5(b)(5)(ii)(C), exchanges should take into account whether granting a spread exemption in a physical commodity derivative would, to the maximum extent practicable, ensure sufficient market liquidity for bona fide hedgers, and not unduly reduce the effectiveness of position limits to diminish, eliminate, or prevent excessive speculation; deter and prevent market manipulation, squeezes, and corners; and ensure that the price discovery function of the underlying market is not disrupted.[863]

Five-Day Rule for Commodity Derivative Contracts in a Physical Commodity Not Subject to Federal Limits

While the Commission's determination regarding the five-day rule is addressed elsewhere,[864] the Commission points out that, as discussed in connection with the definition of bona fide hedging position and in relation to exchange processes under § 150.9, § 150.10, and § 150.11, and as noted above in connection with § 150.5(a), the five-day rule would only apply to certain enumerated positions (pass-through swap offsets, anticipatory, and cross-commodity hedges),[865] rather than when determining whether to recognize as non-enumerated bona fide hedging positions certain non-enumerated hedge strategies for non-referenced contracts. As reproposed, therefore, § 150.5(b) would apply the five-day rule only to pass-through swap offsets, anticipatory, and cross-commodity hedges. However, in regards to exchange processes under § 150.9, § 150.10, and § 150.11, the Commission

recent letters include: CL–CME–61007; CL–ICE–61009; CL–CME–61008; CL–ICE–60929; CL–CME–60926.

[860] The second proviso included in § 150.5(b)(5)(ii)(B) was that the person holding or controlling the positions should not hold or control positions in such spot-month physical-delivery contract.

[861] As noted above, it is the Commission's responsibility under CEA section 4a(a)(3)(B) to set limits, to the maximum extent practicable, in its discretion, that, in addition to ensuring sufficient market liquidity for bona fide hedgers, diminish, eliminate or prevent excessive speculation; deter and prevent market manipulation, squeezes, and corners; and ensure that the price discovery function of the underlying market is not disrupted.

[862] The Commission notes that reproposed § 150.5(b)(5)(ii)(B) retains both of the recommended provisos, although, as noted above, the guidance recommends that such positions should not exceed two times the level of the spot-month limit specified by the exchange that lists the applicable physical-delivery contract, rather than five times.

[863] As noted in the December 2013 Position Limits Proposal, the guidance is consistent with the statutory policy objectives for position limits on physical commodity derivatives in CEA section 4a(a)(3)(B). *See* December 2013 Position Limits Proposal, 78 FR at 38464. The Commission interprets the CEA as providing it with the statutory authority to exempt spreads that are consistent with the other policy objectives for position limits, such as those in CEA section 4a(a)(3)(B). *Id.* CEA section 4a(a)(3)(B) provides that the Commission shall set limits to the maximum extent practicable, in its discretion—to diminish, eliminate, or prevent excessive speculation as described under this section; to deter and prevent market manipulation, squeezes, and corners; to ensure sufficient market liquidity for bona fide hedgers; and to ensure that the price discovery function of the underlying market is not disrupted.

[864] *See* the discussion regarding the five-day rule in connection with the definition of bona fide hedging position and the discussion of § 150.9 (Process for recognition of positions as non-enumerated bona fide hedges).

[865] *See* § 150.1 definition of bona fide hedging position, sections (2)(ii)(A), (3)(iii), (4), and (5) (Other enumerated hedging position). To provide greater clarity as to which bona fide hedging positions the five-day rule applies, the reproposed rules reorganize the definition.

proposes to allow exchanges to waive the five-day rule on a case-by-case basis.

As the Commission cautioned above, exchanges should carefully consider whether to recognize a position as a bona fide hedge or to exempt a spread position held during the last few days of trading in physical-delivery contracts. The Commission points to the tools that exchanges currently use to address concerns during the spot month; as two commenters observed, current tools include requiring gradual reduction of the position (''step down'' requirements) or revoking exemptions to protect the price discovery process in core referenced futures contracts approaching expiration. Consequently, under the reproposed rule, exchanges may recognize positions, on a case-by-case basis in physical-delivery contracts that would otherwise be subject to the five-day rule, as non-enumerated bona fide hedging positions, by applying the exchanges experience and expertise in protecting its own physical-delivery market.

Reporting Requirements for Commodity Derivative Contracts in a Physical Commodity Not Subject to Federal Limits

In response to the comment questioning the proposed reporting requirements by a claim that, ''while the Commission has a surveillance obligation with respect to federal limits, the same obligation has never before existed with respect to exchange-set limits for non-referenced contracts, and does not exist today,'' [866] the Commission points out, as it did in the 2016 Supplemental Position Limits Proposal, that the Futures Trading Act of 1982 ''gave the Commission, under section 4a(5) [since redesignated as section 4a(e)] of the Act, the authority to directly enforce violations of exchange-set, Commission-approved speculative position limits in addition to position limits established directly by the Commission through orders or regulations.'' [867] And, since 2008, it has also been a violation of the Act for any person to violate an exchange position limit rule certified by the exchange.[868] To address any confusion that might have led to such a comment, the Commission reiterates, under CEA section 4a(e), its authority to enforce violations of exchange-set speculative position limits, whether certified or Commission-approved. As the Commission explained in the 2016 Supplemental Position Limits Proposal, exchanges, as SROs, do not act only as independent, private actors.[869] In fact, to repeat the explanation provided by the Commission in 1981, when the Act is read as a whole, ''it is apparent that Congress envisioned cooperative efforts between the self-regulatory organizations and the Commission. Thus, the exchanges, as well as the Commission, have a continuing responsibility in this matter under the Act.'' [870] The 2016 Supplemental Position Limits Proposal pointed out that the ''Commission's approach to its oversight of its SROs was subsequently ratified by Congress in 1982, when it gave the CFTC authority to enforce exchange set limits.'' [871] In addition, as the Commission observed in 2010, and reiterated in the 2016 Supplemental Position Limits Proposal, ''since 1982, the Act's framework explicitly anticipates the concurrent application of Commission and exchange-set speculative position limits.'' [872] The Commission further noted that the ''concurrent application of limits is particularly consistent with an exchange's close knowledge of trading activity on that facility and the Commission's greater capacity for monitoring trading and implementing remedial measures across interconnected commodity futures and option markets.'' [873]

The Commission retains the power to approve or disapprove the rules of exchanges, under standards set out pursuant to the CEA, and to review an exchange's compliance with the exchange's rules, by way of additional examples of the Commission's continuing responsibility in this matter under the Act.

v. Commission Determination Regarding § 150.5(c)

As noted above, in an overall non-substantive change made in reproposing § 150.5, the Commission moved all provisions applying to excluded commodities from § 150.5(b) into reproposed § 150.5(c) to provide greater clarity regarding which provisions concern excluded commodities. The Commission has determined to repropose the rule largely as proposed for excluded commodities (previously under § 150.5(b)), for the reasons noted above, with certain changes discussed below.[874]

Limit Levels for Excluded Commodities

The Commission is reproposing the provisions under § 150.5(c)(1) regarding levels of limits for excluded commodities as modified and reproposed under § 150.5(b)(1),[875] to reference excluded commodities and to remove provisions that were solely addressed to agricultural commodities.[876] These provisions generally provide guidance rather than rigid requirements; the guidance for levels of limits remains the same for

[866] CL–CME–60926 at 15.

[867] 2016 Supplemental Position Limits Proposal, 81 FR at 38466, n. 85 (quoting the Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations, 75 FR 4144, 4145 (Jan. 36, 2010)).

[868] *See* Futures Trading Act of 1982, Public Law 97–444, 96 Stat. 2299–30 (1983) (amending CEA section 4a by including, in what was then a new CEA section 4a(5), since been re-designated as CEA section 4a(e) ''. . . It shall be a violation of this chapter for any person to violate any bylaw, rule, regulation, or resolution of any contract market, derivatives transaction execution facility, or other board of trade licensed, designated, or registered by the Commission or electronic trading facility with respect to a significant price discovery contract fixing limits on the amount of trading which may be done or positions which may be held by any person under contracts of sale of any commodity for future delivery or under options on such contracts or commodities, if such bylaw, rule, regulation, or resolution has been approved by the Commission or certified by a registered entity pursuant to section 7a–2(c)(1) of this title: Provided, That the provisions of section 13(a)(5) of this title shall apply only to those who knowingly violate such limits.'').

[869] 2016 Supplemental Position Limits Proposal, 81 FR at 38465–66.

[870] Establishment of Speculative Position Limits, 46 FR 50938, 50939 (Oct. 16, 1981). As the Commission noted at that time that ''[s]ince many exchanges have already implemented their own speculative position limits on certain contracts, the new rule merely effectuates completion of a regulatory philosophy the industry and the Commission appear to share.'' *Id.* at 50940.

[871] 2016 Supplemental Position Limits Proposal, 81 FR at 38466. See also Futures Trading Act of 1982, Public Law 97–444, 96 Stat. 2299–30 (1983). In 2010, the Commission noted that the 1982 legislation ''also gave the Commission, under section 4a(5) of the Act, the authority to directly enforce violations of exchange-set, Commission-approved speculative position limits in addition to position limits established directly by the Commission through orders or regulations.'' Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations, 75 FR 4144, 4145 (Jan. 36, 2010) (''2010 Position Limits Proposal for Referenced Energy Contracts''). Section 4a(5) has since been re-designated as section 4a(e) of the Act.

[872] 2010 Position Limits for Referenced Energy Contracts at 4145; *see also* 2016 Supplemental Position Limits Proposal, 81 FR at 38466.

[873] *See* 2010 Position Limits for Referenced Energy Contracts, 75 FR at 4145; *see also* 2016 Supplemental Position Limits Proposal, 81 FR at 38466.

[874] The Commission is reproposing the following sections without further discussion, for the reasons provided above, because it received no substantive comments: § 150.5(c)(6) (Pre-enactment and transition period swap positions), § 150.5(c)(7) (Pre-existing positions), and § 150.5(b)(9) (Additional acceptable practices).

[875] As reproposed, § 150.5(c)(1)(iii), like § 150.5(b)(1)(iii), provides that the spot-month, individual non-spot month, and all-months combined limit levels should be ''comparable'' rather than the ''same.''

[876] *See supra* for discussion of the modifications made to the reproposed provisions of § 150.5(b)(1) as compared to the December 2103 Position Limits Proposal; the explanation provided above also pertains to the inclusion of those modifications in reproposed § 150.5(c)(1).

excluded commodities as for all other commodity derivative contracts that are not subject to the limits set forth in reproposed § 150.2, including derivative contracts in a physical commodity as defined in reproposed § 150.1.

Similarly, as to adjustment of limit levels for excluded commodity derivative contracts under § 150.5(c)(2), the reproposed provisions are modified to reference only excluded commodities and to remove provisions that were solely addressed to agricultural commodities. As reproposed, § 150.5(c)(2)(i) provides guidance that the spot month position limits for excluded commodity derivative contracts ''should be maintained at a level that is necessary and appropriate to reduce the potential threat of market manipulation or price distortion of the contract's or the underlying commodity's price or index.''

The Commission did not receive comments regarding § 150.5(c)(3). The guidance in § 150.5(c)(3), on exchange adoption of position accountability levels in lieu of speculative position limits, has been reproposed as was previously proposed in § 150.5(b)(3), modified to remove provisions under § 150.5(b)(3)(i), which were solely addressed to physical commodity derivative contracts, and to reference excluded commodities.

As to the calculation of open interest for use in setting exchange-set speculative position limits for excluded commodities, the Commission is reproposing, in § 150.5(c)(4), the same guidance for excluded commodities that is being reproposed under § 150.5(b)(4) as for all other commodity derivative contracts that are not subject to the limits set forth in § 150.2, including the modification to provide that a DCM or SEF that is a trading facility would include swaps in its open interest calculation only if such entity is required to administer position limits on swap contracts of its facility.

Exchange—Administered Exemptions for Excluded Commodities

In regards to hedge exemptions, the Commission is reproposing in new § 150.5(c)(5)(i) for contracts in excluded commodities a modification of what was previously proposed in § 150.5(b)(5)(i) that eliminates the guidance that exchanges ''may provide for recognition of a non-enumerated bona fide hedge in a manner consistent with the process described in § 150.9(a).'' That provision was intended to apply only to physical commodity contracts and not to exemptions granted by exchanges for contracts in excluded commodities.[877]

As noted above, in reproposing the definition of bona fide hedging position, the Commission is clarifying that an exchange may otherwise recognize as bona fide any position in a commodity derivative contract in an excluded commodity, so long as such recognition is pursuant to such exchange's rules. Although the Commission's standards in the December 2013 Position Limits Proposal applied the incidental test and the orderly trading requirements to all commodities, the Commission, as previously described, proposed in the 2016 Supplemental Position Limits Proposal to remove both those standards from the definition of bona fide hedging position.[878] Moreover, the reproposed definition of bona fide hedging position would provide only that the position is either: (i) Enumerated in the definition (in paragraphs (3), (4), or (5)) and meets the economically appropriate test; or (ii) recognized by an exchange under rules previously submitted to the Commission.[879] The Commission's standards for recognizing a position as a bona fide hedge in an excluded commodity, therefore, would not include the additional requirements applicable to physical commodities subject to federal limits. Consequently, as reproposed, the exchanges would have reasonable discretion to comply with core principles regarding position limits on excluded commodities so long as the exchange does so pursuant to exchange rules previously submitted to the Commission under Part 40.

In addition, in conjunction with the amendments to the definition of bona fide hedging positions in regards to excluded commodities,[880] the Commission is reproposing § 150.5(c)(5)(ii), proposed as § 150.5(b)(5)(ii)(D) in the 2016 Supplemental Position Limits Proposal, with no further modification, to afford greater flexibility for exchanges when granting exemptions for excluded commodities. The 2016 Supplemental Position Limits Proposal provided, in addition to granting exemptions under paragraphs (b)(5)(ii)(A), (b)(5)(ii)(B), and (b)(5)(ii)(C) of § 150.5, that exchanges may grant a ''limited'' risk management exemptions pursuant to rules consistent with the guidance in Appendix A of part 150. As reproposed, § 150.5(c)(5)(ii) eliminates the modifier ''limited'' from the risk management exemptions, and provides merely that exchanges may grant, in addition to the exemptions under paragraphs (b)(5)(ii)(A), (b)(5)(ii)(B), and (b)(5)(ii)(C), risk management exemptions pursuant to rules submitted to the Commission, ''including'' for a position that is consistent with the guidance in Appendix A of part 150.

In regards to the provisions addressing applications for exemptions for positions in excluded commodities, the Commission is modifying what was copied from § 150.5(b)(5)(iii) to provide, under § 150.5(c)(5)(iii), simply that an exchange may allow a person to file an exemption application for excluded commodities after the person assumes the position that exceeded a position limit.

Finally, in reproposing the aggregation provision for excluded commodities under § 150.5(c)(8), the Commission is not merely mirroring the aggregation provision as previously proposed in § 150.5(b)(8). As noted above, the reproposed aggregation provisions for physical commodity derivatives contracts, whether under § 150.5(a)(8) or § 150.5(b)(8), provide that exchanges must have aggregation provisions that conform to § 150.4. Reproposed § 150.5(c)(8), consistent with the rest of reproposed § 150.5(c), would instead provide guidance, that exchanges ''should'' have aggregation rules for excluded commodity derivative contracts that conform to § 150.4.

*E. Part 19—Reports by Persons Holding Bona Fide Hedge Positions Pursuant to § 150.1 of This Chapter and by Merchants and Dealers in Cotton*

1. Current Part 19

The market and large trader reporting rules are contained in parts 15 through 21 of the Commission's regulations.[881] Collectively, these reporting rules effectuate the Commission's market and financial surveillance programs by enabling the Commission to gather information concerning the size and composition of the commodity futures, options, and swaps markets, thereby permitting the Commission to monitor and enforce the speculative position

[877] In addition, as noted above, the Commission is reproposing § 150.5(b)(5)(i) with a modification that clarifies that this provision is guidance in the case of commodity derivatives contracts in a physical commodity not subject to federal limits.

[878] *See* 2016 Supplemental Position Limits Proposal, definition of bona fide hedging position (amending the definition previously proposed in the December 2013 Position Limits Proposal), 78 FR at 38463–64, 38505–06.

[879] The economically appropriate test has historically been interpreted primarily in the context of physical commodities, rather than applied to excluded commodities.

[880] In each case pursuant to rules submitted to the Commission, consistent with the guidance in Appendix A of this part.

[881] 17 CFR parts 15–21.

limits that have been established, among other regulatory goals. The Commission's reporting rules are implemented pursuant to the authority of CEA sections 4g and 4i, among other CEA sections. Section 4g of the Act imposes reporting and recordkeeping obligations on registered entities, and obligates FCMs, introducing brokers, floor brokers, and floor traders to file such reports as the Commission may require on proprietary and customer positions executed on any board of trade.[882] Section 4i of the Act requires the filing of such reports as the Commission may require when positions equal or exceed Commission-set levels.[883]

Current part 19 of the Commission's regulations sets forth reporting requirements for persons holding or controlling reportable futures and option positions ''which constitute bona fide hedging positions as defined in [§] 1.3(z)'' and for merchants and dealers in cotton holding or controlling reportable positions for future delivery in cotton.[884] In the several markets with federal speculative position limits—namely those for grains, the soy complex, and cotton—hedgers that hold positions in excess of those limits must file a monthly report pursuant to part 19 on *CFTC Form 204: Statement of Cash Positions in Grains,*[885] which includes the soy complex, and *CFTC Form 304 Report: Statement of Cash Positions in Cotton.*[886] These monthly reports, collectively referred to as the Commission's ''series '04 reports,'' must show the trader's positions in the cash market and are used by the Commission to determine whether a trader has sufficient cash positions that justify futures and option positions above the speculative limits.[887]

2. Amendments to Part 19

In the December 2013 Position Limits Proposal, the Commission proposed to amend part 19 so that it would conform to the Commission's proposed changes to part 150.[888] First, the Commission proposed to amend part 19 by adding new and modified cross-references to proposed part 150, including the new definition of bona fide hedging position in proposed § 150.1. Second, the Commission proposed to amend § 19.00(a) by extending reporting requirements to any person claiming any exemption from federal position limits pursuant to proposed § 150.3. The Commission proposed to add new series '04 reporting forms to effectuate these additional reporting requirements. Third, the Commission proposed to update the manner of part 19 reporting. Lastly, the Commission proposed to update both the type of data that would be required in series '04 reports as well as the timeframe for filing such reports.

*Comments Received:* One commenter acknowledges concerns presented by Commission staff at the Staff Roundtable that exemptions from position limits be limited to prevent abuse, but does not believe that the adoption of additional recordkeeping or reporting rules or the development of costly infrastructure is required because statutory and regulatory safeguards already exist or are already proposed in the December 2013 Position Limits Proposal, noting that: (i) The series '04 forms as well as DCM exemption documents will be required of market participants, who face significant penalties for false reporting, and the Commission may request additional information if the information provided is unsatisfactory; and (ii) market participants claiming a bona fide hedging exemption are still subject to anti-disruptive trading prohibitions in CEA section 4c(a)(5), anti-manipulation prohibitions in CEA sections 6(c) and 9(c), the orderly trading requirement in proposed § 150.1, and DCM oversight. The commenter stated that these requirements comprise a ''thorough and robust regulatory structure'' that does not need to be augmented with new recordkeeping, reporting, or other obligations to prevent misuse of hedging exemptions.[889] A second commenter echoed that additional recordkeeping or reporting obligations are unnecessary and would create unnecessary regulatory burdens.[890]

Another commenter stated that the various forms required by the regime, while not lengthy, represent significant data collection and categorization that will require a non-trivial amount of work to accurately prepare and file. The commenter claimed that a comprehensive position limits regime could be implemented with a ''far less burdensome'' set of filings and requested that the Commission review the proposed forms and ensure they are ''as clear, limited, and workable'' as possible to reduce burden. The commenter stated that it is not aware of any software vendors that currently provide solutions that can support a commercial firm's ability to file the proposed forms.[891]

One commenter recommended that the Commission eliminate the series '04 reports in light of the application and reporting requirements laid out in the 2016 Supplemental Position Limits Proposal. The commenter asserted that the application requirements are in addition to the series '04 forms, which the commenter claims ''only provide the Commission with a limited surveillance benefit.'' [892] Another commenter raised concerns regarding forms filed under part 19 and the data required to be filed with exchanges under §§ 150.9–11. The commenter stated that the 2016 Supplemental Position Limits Proposal requires that ''those exceeding the federal limits file the proposed forms including Form 204'' but lacks ''meaningful guidance'' regarding the data that must be maintained ''effectively in real-time'' to populate the forms.[893]

Several commenters requested that the Commission create user-friendly guidebooks for the forms so that all entities can clearly understand any required forms and build the systems to file such forms, including providing workshops and/or hot lines to improve the forms.[894]

One commenter expressed concern for reporting requirements in conflict with other regulatory requirements (such as FASB ASC 815).[895]

Finally, two commenters recommended modifying or removing the requirement to certify series '04 reports as ''true and correct''. One commenter suggested that the requirement be removed due to the difficulty of making such a certification

[882] *See* CEA section 4g(a); 7 U.S.C. 6g(a).

[883] *See* CEA section 4i; 7 U.S.C. 6i.

[884] *See* 17 CFR part 19. Current part 19 cross-references a provision of the definition of reportable position in 17 CFR 15.00(p)(2). As discussed below, that provision would be incorporated into proposed § 19.00(a).

[885] Current *CFTC Form 204: Statement of Cash Positions in Grains* is available at *http://www.cftc.gov/ucm/groups/public/@forms/documents/file/cftcform204.pdf.*

[886] Current *CFTC Form 304 Report: Statement of Cash Positions in Cotton* is available at *http://www.cftc.gov/ucm/groups/public/@forms/documents/file/cftcform304.pdf.*

[887] In addition, in the cotton market, merchants and dealers file a weekly CFTC Form 304 Report of their unfixed-price cash positions, which is used to publish a weekly Cotton On-call report, a service to the cotton industry. The Cotton On-Call Report shows how many unfixed-price cash cotton purchases and sales are outstanding against each cotton futures month.

[888] *See* December 2013 Position Limits Proposal, 78 FR at 75741–75746.

[889] CL–Working Group–59959 at 3–4.

[890] CL–NFP–60393 at 15–16.

[891] CL–COPE–59662 at 24; CL–COPE–60932 at 10; CL–EEI–EPSA–60925 at 9.

[892] CL–FIA–60937 at 17.

[893] CL–EEI–EPSA–60925 at 9.

[894] CL–COPE–59662 at 24; CL–COPE–60932 at 10; CL–ASR–60933 at 4; CL–Working Group–60947 at 17–18; CL–EEI–EPSA–60925 at 3.

[895] CL–U.S. Dairy–59597 at 6.

and the fact that CEA section 6(c)(2) already prohibits the submission of false or misleading information.[896] Another noted that the requirement to report very specific information relating to hedges and cash market activity involves data that may change over time. The commenter suggested the Commission adopt a good-faith standard regarding ''best effort'' estimates of the data when verifying the accuracy of Form 204 submissions and, assuming the estimate of physical activity does not otherwise impact the bona fide hedge exemption (*e.g.* cause the firm to lose the exemption), not penalize entities for providing the closest approximation of the position possible.[897]

*Commission Reproposal:* The Commission responds to specific comments regarding the content and timing of the series '04 forms and other concerns below. The Commission agrees with the commenters that the forms should be clear and workable, and offers several clarifications and amendments below in response to comments about particular aspects of the series '04 reports.

The Commission notes that the information required on the series '04 reports represents a trader's most basic position data, including the number of units of the cash commodity that the firm has purchased or sold, or the size of a swap position that is being offset in the futures market. The Commission believes this information is readily available to traders, who routinely make trading decisions based on the same data that is required on the series '04 reports. The Commission is proposing to move to an entirely electronic filing system, allowing for efficiencies in populating and submitting forms that require the same information every month. Most traders who are required to file the series '04 reports must do so for only one day out of the month, further lowering the burden for filers. In short, the Commission believes potential burdens under the Reproposal have been reduced wherever possible while still providing adequate information for the Commission's Surveillance program. For market participants who may require assistance in monitoring for speculative position limits and gathering the information required for the series '04 reports, the Commission is aware of several software companies who, prior to the vacation of the Part 151 Rulemaking, produced tools that could be useful to market participants in fulfilling their compliance obligations under the new position limits regime.

The Commission notes that the reporting obligations proposed in the 2016 Supplemental Position Limits Proposal are intended to be complimentary to, not duplicative of, the series '04 reporting forms. In particular, the Commission notes the distinction between Form 204 enumerated hedging reporting and exchange-based non-enumerated hedging reporting. The 2016 Supplemental Position Limits Proposal provides exchanges with the authority to require reporting from market participants. That is, regarding an exchange's process for non-enumerated bona fide hedging position recognition, the exchange has discretion to implement any additional reporting that it may require. The Commission declines to eliminate series '04 reporting in response to the commenters because, as noted throughout this section, the data provided on the forms is critical to the mission of the Commission's Surveillance program to detect and deter manipulation and abusive trading practices in physical commodity markets.

In response to the commenters that requested guidebooks for the series '04 reporting forms, the Commission believes that it is less confusing to ensure that form instructions are clear and detailed than it is to provide generalized guidebooks that may not respond to specific issues. The Commission has clarified the sample series '04 forms found in Appendix A to part 19, including instructions to such forms, and invites comments in order to avoid future confusion. Specifically, the Commission has added instructions regarding how to fill out the trader identification section of each form; reorganized instructions relating to individual fields on each form; edited the examples of each form to reduce confusion and match changes to information required as described in this section; and clarified the authority for the certifications made on the signature/authorization page of each form.

The Commission's longstanding experience with collecting and reviewing Form 204 and Form 304 has shown that many questions about the series '04 reports are specific to the circumstances and trading strategies of an individual market participant, and do not lend themselves to generalization that would be helpful to many market participants.

The Commission also notes, in response to the commenter expressing concerns about other regulatory requirements, the policy objectives and standards for hedging under financial accounting standards differ from the statutory policy objectives and standards for hedging under the Act. Because of this, reporting requirements, and the associated burdens, would also differ between the series '04 reports and accounting statements.

Finally, the Commission is proposing to amend the certification language found at the end of each form to clarify that the certification requires nothing more than is already required of market participants in section 6(c)(2) of the Act. In response to the commenters' request for a ''best effort'' standard, the Commission added the phrase ''to the best of my knowledge'' preceding the certification from the authorized representative of the reporting trader that the information on the form is true and correct. The Commission has also added instructions to each form clarifying what is required on the signature/authorization page of each form. The Commission notes that, in the recent past, the Division of Market Oversight has issued advisories and guidance on proper filing of series '04 reports, and the Division of Enforcement has settled several cases regarding lack of accuracy and/or timeliness in filing series '04 forms.[898] The Commission believes the certification language is an important reminder to reporting traders of their responsibilities to file accurate information under several sections of the Act, including but not limited to CEA section 6(c)(2).

a. Amended cross references

*Proposed Rule:* As discussed above, in the December 2013 Position Limits Proposal, the Commission proposed to replace the definition of bona fide hedging transaction found in § 1.3(z) with a new proposed definition of bona fide hedging position in proposed § 150.1. As a result, proposed part 19 would replace cross-references to § 1.3(z) with cross-references to the new definition of bona fide hedging positions in proposed § 150.1.

The Commission also proposed expanding Part 19 to include reporting requirements for positions in swaps, in addition to futures and options positions, for any part of which a person relies on an exemption. To accomplish this, ''positions in commodity derivative contracts,'' as defined in proposed § 150.1, would replace ''futures and option positions'' throughout amended

[896] *See* CL–CMC–59634 at 17.

[897] CL–Working Group–59693 at 65.

[898] *See, e.g.,* ''Obligation of Reportable Market Participants to File CFTC Form 204 Reports,'' CFTC Staff Advisory 13–42, July 8, 2013; and CFTC Dockets Nos. 16–21, 15–41, 16–07, 16–20.

part 19 as shorthand for any futures, option, or swap contract in a commodity (other than a security futures product as defined in CEA section 1a(45)).[899] This amendment was intended to harmonize the reporting requirements of part 19 with proposed amendments to part 150 that encompass swap transactions.

Proposed § 19.00(a) would eliminate the cross-reference to the definition of reportable position in § 15.00(p)(2). The Commission noted that the current reportable position definition essentially identifies futures and option positions in excess of speculative position limits. Proposed § 19.00(a) would simply make clear that the reporting requirement applies to commodity derivative contract positions (including swaps) that exceed speculative position limits, as discussed below.

*Comments Received:* The Commission received no comments on the proposed cross-referencing amendments.

*Commission Reproposal:* The Commission is repurposing the amended cross-references in part 19, as originally proposed.

b. Persons required to report—§ 19.00(a)

*Proposed Rule:* Because the reporting requirements of current part 19 apply only to persons holding bona fide hedge positions and merchants and dealers in cotton holding or controlling reportable positions for future delivery in cotton, the Commission proposed to extend the reach of part 19 by requiring all persons who wish to avail themselves of any exemption from federal position limits under proposed § 150.3 to file applicable series '04 reports.[900] The Commission also proposed to require that anyone exceeding a federal limit who has received a special call related to part 150 must file a series '04 form. Collection of this information would facilitate the Commission's surveillance program with respect to detecting and deterring trading activity that may tend to cause sudden or unreasonable fluctuations or unwarranted changes in the prices of the referenced contracts and their underlying commodities. By broadening the scope of persons who must file series '04 reports, the Commission seeks to ensure that any person who claims any exemption from federal speculative position limits can demonstrate a legitimate purpose for doing so.

Series '04 reports currently refers to Form 204 and Form 304, which are listed in current § 15.02.[901] The Commission proposed to add three new series '04 reporting forms to effectuate the expanded reporting requirements of part 19.[902] Proposed Form 504 would be added for use by persons claiming the conditional spot-month limit exemption pursuant to proposed § 150.3(c).[903] Proposed Form 604 would be added for use by persons claiming a bona fide hedge exemption for either of two specific pass-through swap position types, as discussed further below.[904] Proposed Form 704 would be added for use by persons claiming a bona fide hedge exemption for certain anticipatory bona fide hedging positions.[905]

*Comments Received:* The Commission received no comments on proposed § 19.00(a) regarding who must file series '04 reports.

*Commission Reproposal:* The Commission is reproposing the expansion of § 19.00(a), as originally proposed.

c. Manner of reporting—§ 19.00(b)

i. Excluding certain source commodities, products or byproducts of the cash commodity hedged—§ 19.00(b)(1)

*Proposed Rule:* For purposes of reporting cash market positions under current part 19, the Commission historically has allowed a reporting trader to ''exclude certain products or byproducts in determining his cash positions for bona fide hedging'' if it is ''the regular business practice of the reporting trader'' to do so.[906] The Commission has proposed to clarify the meaning of ''economically appropriate'' in light of this reporting exclusion of certain cash positions.[907] Therefore, in the December 2013 Position Limits Proposal, the Commission proposed in § 19.00(b)(1) that a source commodity itself can only be excluded from a calculation of a cash position if the amount is de minimis, impractical to account for, and/or on the opposite side of the market from the market participant's hedging position.[908]

The Commission explained in the December 2013 Position Limits Proposal that the original part 19 reporting exclusion was intended to cover only cash positions that were not capable of being delivered under the terms of any derivative contract, an intention that ultimately evolved to allow cross-commodity hedging of products and byproducts of a commodity that were not necessarily deliverable under the terms of any derivative contract. The Commission also noted that the instructions on current Form 204 go further than current § 19.00(b)(1) by allowing the exclusion of certain source commodities in addition to products and byproducts, when it is the firm's normal business practice to do so.

*Comments Received:* One commenter suggested the Commission expand the provision in proposed § 19.00(b)(1) that allows a reporting person to exclude source commodities, products or byproducts in determining its cash position for bona fide hedging to allow a person to also exclude inventory and contracts of the actual commodity in the course of his or her regular business practice. The commenter also noted that proposed § 19.00(b)(1) only permits this exclusion if the amount is de minimis, despite there being ''many circumstances'' that make the inclusion of such source commodities irrelevant for reporting purposes. The commenter requested that the Commission only require a reporting person to calculate its cash positions in accordance with its regular business practice and report the

[899] *See* discussion above.

[900] *See* 17 CFR part 19. Current part 19 cross-references the definition of reportable position in 17 CFR 15.00(p).

[901] 17 CFR 15.02.

[902] As noted in the December 2013 Position Limits Proposal, the Commission is avoiding the use of any form numbers with ''404'' to avoid confusion with the part 151 Rulemaking, which required Forms 404, 404A, and 404S. *See* December 2013 Position Limits Proposal, 78 FR at 75742.

[903] *See supra* discussion of proposed § 150.3(c).

[904] Proposed Form 604 would replace Form 404S (as contemplated in vacated part 151).

[905] The updated definition of bona fide hedging in proposed § 150.1 incorporates several specific types of anticipatory transactions: Unfilled anticipated requirements, unsold anticipated production, anticipated royalties, anticipated services contract payments or receipts, and anticipatory cross-commodity hedges. *See* paragraphs (3)(iii), (4)(i), (4)(iii), (4)(iv) and (5), respectively, of the Commission's amended definition of bona fide hedging transactions in proposed § 150.1 as discussed *above.*

[906] *See* 17 CFR 19.00(b)(1) (providing that ''[i]f the regular business practice of the reporting trader is to exclude certain products or byproducts in determining his cash position for bona fide hedging . . . ., the same shall be excluded in the report'').

[907] *See supra* discussion of the ''economically appropriate test'' as it relates to the definition of bona fide hedging position. In order for a position to be economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise, the enterprise generally should take into account all inventory or products that the enterprise owns or controls, or has contracted for purchase or sale at a fixed price. For example, in line with its historical approach to the reporting exclusion, the Commission does not believe that it would be economically appropriate to exclude large quantities of a source commodity held in inventory when an enterprise is calculating its value at risk to a source commodity and it intends to establish a long derivatives position as a hedge of unfilled anticipated requirements.

[908] Proposed § 19.00(b)(1) adds a caveat to the alternative manner of reporting: When reporting for the cash commodity of soybeans, soybean oil, or soybean meal, the reporting person shall show the cash positions of soybeans, soybean oil and soybean meal. This proposed provision for the soybean complex is included in the current instructions for preparing Form 204.

cash positions that it considered in making its bona fide hedging determinations.[909]

*Commission Reproposal:* The Commission is reproposing § 19.00(b)(1), as originally proposed, because the Commission is concerned that adopting the commenter's request could lead to ''cherry-picking'' a cash market position in an attempt to justify a speculative position as a hedge. As noted in the December 2013 Position Limits Proposal, the Commission's clarification of the § 19.00(b)(1) reporting exclusion was proposed to prevent the definition of bona fide hedging positions in proposed § 150.1 from being swallowed by this reporting rule. The Commission stated ''. . . it would not be economically appropriate behavior for a person who is, for example, long derivative contracts to exclude inventory when calculating unfilled anticipated requirements. Such behavior would call into question whether an offset to unfilled anticipated requirements is, in fact, a bona fide hedging position, since such inventory would fill the requirement. As such, a trader can only underreport cash market activities on the opposite side of the market from her hedging position as a regular business practice, unless the unreported inventory position is de minimis or impractical to account for.'' [910] If a person were only required to report cash positions that are offset by particular derivative positions, then the form would not provide an indication as to whether the derivative position is economically appropriate to the reduction of risk, making the inclusion of source commodities very relevant for reporting purposes, contrary to the commenter's suggestion.

Because of these and other concerns, market participants have historically been required to report cash market information in aggregate form for the commodity as a whole, not the ''line item'' style of hedge reporting requested by the commenter (where firms report cash trades by category, tranche, or corresponding futures position). Further, since it is important for Surveillance purposes to receive a snapshot of a market participant's cash market position, the series '04 forms currently require a market participant to provide relevant inventories and fixed price contracts in the hedged (or cross-hedged) commodity. The Commission believes it is necessary to maintain this aggregate reporting in order for the Commission's Surveillance program to properly monitor for position limit violations and to prevent market manipulation.

Further, the Commission believes that firms may find reporting an aggregate cash market position less burdensome than attempting to identify portions of that position that most closely align with individual hedge positions as, according to some commenters, many firms hedge on a portfolio basis, making identifying the particular hedge being used difficult.[911]

ii. Cross-commodity Hedges, Standards and Conversion Factors—§ 19.00(b)(2)–(3)

*Proposed Rules:* In the December 2013 Position Limits Proposal, the Commission proposed under § 19.00(b)(2) instructions for reporting a cash position in a commodity that is different from the commodity underlying the futures contract used for hedging.[912] The Commission also proposed to maintain the requirement in § 19.00(b)(3) that standards and conversion factors used in computing cash positions for reporting purposes must be made available to the Commission upon request.[913] The Commission clarified that such information would include hedge ratios used to convert the actual cash commodity to the equivalent amount of the commodity underlying the commodity derivative contract used for hedging, and an explanation of the methodology used for determining the hedge ratio. Finally, the Commission provided examples of completed series '04 forms in proposed Appendix A to part 19 along with blank forms and instructions.[914]

*Comments Received:* The Commission received no comments on proposed §§ 19.00(b)(2)–(3).

*Commission Reproposal:* The Commission is reproposing §§ 19.00(b)(2)–(3), as originally proposed.

d. Information Required—§ 19.01(a)

i. Bona Fide Hedgers Reporting on Form 204—§ 19.01(a)(3)

*Proposed Rule:* Current § 19.01(a) sets forth the data that must be provided by bona fide hedgers (on Form 204) and by merchants and dealers in cotton (on Form 304). The Commission proposed to continue using Forms 204 and 304, which will feature only minor changes to the types of data to be reported under § 19.01(a)(3).[915] These changes include removing the modifier ''fixed price'' from ''fixed price cash position;'' requiring cash market position information to be submitted in both the cash market unit of measurement (*e.g.* barrels or bushels) and futures equivalents; and adding a specific request for data concerning open price contracts to accommodate open price pairs. In addition, the monthly reporting requirements for cotton, including the granularity of equity, certificated and non-certificated cotton stocks, would be moved to Form 204, while weekly reporting for cotton would be retained as a separate report made on Form 304 in order to maintain the collection of data required by the Commission to publish its weekly public cotton ''on call'' report.

*Comments Received:* The Commission received several comments regarding the proposed revisions to Form 204. These comments can be grouped loosely into three categories: general comments on bona fide hedge reporting; comments regarding the general information required on Form 204; and comments regarding the more specific nature of the cash market information required to be reported. The Commission responds to each category separately below.

*Comments:* One commenter stated that CFTC should reduce the complexity and compliance burden of bona fide hedging record keeping and reporting by using a model similar to the current exchange-based exemption process.[916] The commenter also stated that the requirement to keep records and file reports, in futures equivalents, regarding the commercial entity's cash market contracts and derivative market positions on a real-time basis globally, will be complex and impose a significant compliance burden. The

[909] *See* CL–Working Group–60396 at 16–17; CL–Working Group–60947 at 15–17.

[910] *See* December 2013 Position Limits Proposal, 78 FR at 75743. The Commission provided an example: ''By way of example, the alternative manner of reporting in proposed § 19.00(b)(1) would permit a person who has a cash inventory of 5 million bushels of wheat, and is short 5 million bushels worth of commodity derivative contracts, to underreport additional cash inventories held in small silos in disparate locations that are administratively difficult to count.'' This person could instead opt to calculate and report these hard-to-count inventories and establish additional short positions in commodity derivative contracts as a bona fide hedge against such additional inventories.

[911] *See* CL-Working Group-59693 at 65.

[912] *See* December 2013 Position Limits Proposal, 78 FR at 75743. The proposed § 19.00(b)(2) is consistent with provisions in the current section, but would add the term commodity derivative contracts (as defined in proposed § 150.1). The proposed definition of cross-commodity hedge in proposed § 150.1 is discussed *above.*

[913] *See* December 2013 Position Limits Proposal, 78 FR at 75743.

[914] *Id.*

[915] The list of data required for persons filing on Forms 204 and 304 has been relocated from current § 19.01(a) to proposed § 19.01(a)(3).

[916] CL–ASR–59668 at 3.

commenter noted such records are not needed for commercial purposes.[917]

One commenter requested that the Commission provide for a single hedge exemption application and reporting process, and should not require applicants to file duplicative forms at the exchange and at the Commission. The commenter noted its support for rules that would delegate, to the exchanges, (1) the hedge exemption application and approval process, and (2) hedge exemption reporting (if any is required). The commenter argued that the exchanges, rather than the Commission, have a long history with enforcing position limits on all of their contracts and are in a much better position than the Commission to judge the applicant's hedging needs and set an appropriate hedge level for the hedge being sought. Thus, the commenter suggested, the exchanges should be the point of contact for market participants seeking hedge exemptions.[918]

One commenter requested that the Commission address all pending requests for CEA 4a(a)(7) exemptions and respond to all requests for bona fide hedging exemptions from the energy industry.[919]

*Commission Reproposal:* In response to the first commenter, the Commission notes that, while the exchange referred to by the commenter does not have a reporting process analogous to Form 204, it does require an application prior to the establishment of a position that exceeds a position limit. In contrast, advance notice is not required for most federal enumerated bona fide hedging positions.[920] In the Commission's experience, the series '04 reports have been useful and beneficial to the Commission's Surveillance program and the Commission finds no compelling reason to change the forms to conform to the exchange's process. Further, the Commission notes that Form 204 is filed once a month as of the close of business of the last Friday of the month; it is not and has never been required to be filed on a real-time basis globally. A market participant only has to file Form 204 if it is over the limit at any point during the month, and the form requires only cash market activity (not derivatives market positions).

The second commenter was responding to questions raised at the Energy and Environmental Markets Advisory Council Meeting in June 2014; the Commission notes in response to that commenter that there is no federal exemption application process for most enumerated hedges. For non-enumerated hedges and certain enumerated anticipatory hedges, in response to the EEMAC meeting and other comments from market participants, the Commission proposed a single exchange based process for recognizing bona fide hedges for both federal and exchange limits. Under this process, proposed in the 2016 Supplemental Position Limits Proposal, market participants would not be required to file with both the exchange and the Commission.[921]

Finally, in response to the commenter's request that the Commission respond to pending requests for exemptions under CEA section 4a(a)(7), the Commission notes that it responded to the outstanding section 4a(a)(7) requests in the December 2013 Position Limits Proposal. In particular, the Commission proposed to include some of the energy industry's requests in the definition of bona fide hedging position and declined to include other requests.[922]

*Comments:* One commenter recommended that the Commission clarify that column three of Form 204 should permit a market participant to identify the number of futures-equivalent referenced contracts that hedge an identified amount of cash-market positions, but without separately identifying the positions in each referenced contract. The commenter stated that separate identification would add to the financial burden, but that it does not believe that it adds any benefit to the Commission.[923] Two commenters also recommended the Commission remove from Form 204 the requirement for reporting non-referenced contracts, noting that the Commission did not explain why a market participant should report commodity derivative contracts that are not referenced contracts.[924]

One commenter also recommended that the Commission either delete or make optional the identification of a particular enumerated position in column two of Section A or provide a good-faith standard. The commenter claimed that many energy firms hedge on a portfolio basis, and would not be able to identify a particular enumerated position that applies to the referenced contract position needing bona fide hedging treatment.[925]

One commenter asked for clarification regarding whether Section C of Form 204, which requires information regarding cotton stocks, is required of market participants in all commodities or just those in cotton markets.[926]

One commenter recommended that the Commission remove the requirement in Form 204 to submit futures-equivalent derivative positions, stating that the Commission did not explain why it needs to obtain data on a market participant's futures-equivalent position as part of proposed Form 204 in light of the presumption that the Commission already has a market participant's future-equivalent position from large-trader reporting rules and access to SDR data.[927] Another commenter noted that Form 204 mixes units of measurement between futures and cash positions and requested the Commission require market participants to use either cash units or futures units. The commenter noted that it's an easy conversion to make but that the ''mix'' of both units is confusing.[928]

*Commission Reproposal:* With respect to the comments regarding column three of Form 204, the Commission clarifies that Form 204 allows filers to identify multiple referenced contracts used for hedging a particular commodity cash position in the same line of Form 204. Because position limits under § 150.2 are to be imposed on referenced contracts, cash positions hedged by such referenced contracts should be reported on an aggregate basis, not separated out by individual contract. However, the Commission declines to adopt the commenters' recommendation to delete the phrase ''Commodity Derivative Contract'' from the title of column three, because § 19.00(a)(3) allows the Commission to require filing of a series '04 form of anyone holding a reportable position under § 15.00(p)(1), which may involve a commodity derivative contract that does not fit the definition of referenced

917 CL–ASR–59668 at 7; CL–ASR–60933 at 5.

918 CL–AGA–59935 at 13.

919 CL–NFP–60393 at 15–16.

920 The Commission notes that advance notice is required for recognition of anticipatory hedging positions by the Commission. *See* below for more discussion of anticipatory hedging reporting requirements.

921 *See supra* the discussion of proposed §§ 150.9 and 150.11.

922 The reasoning behind the Commission's determinations with respect to previous requests for exemption under CEA section 4a(a)(7) is documented in the December 2013 Position Limits Proposal, 78 FR at 75719–75722. *See also* the definition of bona fide hedging position discussed *supra.*

923 CL–FIA–59595 at 38.

924 The Commission notes that the commenters are referring to titular language on column 3 of the example Form 204 found in proposed Appendix A to part 19, which states ''Commodity Derivative Contract or Referenced Contract'' as the information required in that column. CL–FIA–59595 at 38; CL–Working Group–59693 at 65.

925 CL–Working Group–59693 at 65.

926 CL–ASR–60933 at 4.

927 CL–FIA–59595 at 37.

928 CL–ASR–60933 at 4.

contract.[929] Further, the Commission can require a special call respondent to file their response using the relevant series '04 form, and the Form 204 may be filed in order to claim exemptions from §§ 150.3(b) or 150.3(d), exemptions which may not involve a referenced contract. In sum, because the Commission may require the filing of Form 204 for purposes other than bona fide hedging, the form should include both ''Commodity Derivative Contract'' and, separately, ''Referenced Contract'' in the title of column three. To avoid further confusion, the Commission has rephrased the wording of the column title and amended the instructions to the form.

With respect to column two of Form 204, the Commission is proposing to adopt the commenter's recommendation to delete the requirement to identify which paragraphs of the bona fide hedging definition are represented by the hedged position. The requirement seemed to be confusing to commenters who found it unclear whether the column required the identification of all bona fide hedge definition paragraphs used for the total cash market position or the identification of separate cash positions for each paragraph used. While the requirement was intended to provide insight into which enumerated provision of the bona fide hedging definition was being relied upon in order to provide context to the cash position, the column was never intended to prevent multiple paragraphs being cited at once. Given the confusion, the Commission is concerned that the information in column two may not provide the intended information while being burdensome to implement for both market participants and Commission staff. For these reasons, the Commission is proposing to delete column two of Form 204, and has updated the sample forms in Appendix A to part 19 accordingly.

In response to the commenter requesting clarification regarding Section C of Form 204, the Commission confirms that Section C is only required of entities which hold positions in cotton markets that must be reported on Form 204. Further, the Commission proposes that, in order for the Commission to effectively evaluate the legitimacy of a claimed bona fide hedging position, filers of Section C of Form 204 will be required to differentiate between equity stock held in their capacities as merchants, producers, and/or agents in cotton. The Commission has updated Section C of Form 204 and § 19.01(a)(3)(vi)(A) to reflect this change. The Commission does not believe this distinction will create any significant extra burden on cotton merchants, as the Commission understands that many entities in cotton markets will hold equity stocks in just one of the three capacities required on the form.

The Commission notes in response to the last commenter that Form 204 does not require the futures equivalent value of derivative positions but rather the futures equivalent of the cash position underlying a hedged position (*e.g.,* 20,000,000 barrels of crude oil is equivalent to 20,000 futures equivalents, given a 1,000 barrel unit of trading for the futures contract). The futures equivalent of the cash position quantity is not available from any Commission data source because cash positions are not reported to the Commission under, for example, large trader reporting or swap data repository regulations. The Commission is proposing to require firms to report both the cash market unit of measurement and the futures equivalent measurement for a position in order to easily identify the size of the position underlying a hedge position, and has updated § 19.01(a)(3), instructions to the sample Form 204 in Appendix A to part 19, and the field names on the Form 204 itself to clarify this requirement. The Commission agrees with the commenter that it is an easy conversion to make, and does not anticipate that this requirement will create any significant extra burden on market participants. Obtaining the futures equivalent information directly from the market participant—as opposed to calculating it upon receipt of the form—is necessary particularly with respect to cross-commodity hedging where calculating the hedging ratio may not be as clear-cut. In its experience administering and collecting Form 204, the Commission has noted much confusion regarding whether cash market information should be reported in futures equivalents or in cash market units. Currently, the form requires cash market units, but the Commission has seen both units of measurement used (sometimes on the same form), which requires Commission staff to contact traders in order to validate the numbers on the form. The Commission is proposing to require both in order to avoid such confusion.

*Comment:* One commenter proposed modifications to the information required to be reported on Form 204. Specifically, the commenter suggested that the filer should be required to report the aggregate quantity of cash positions that underlie bona fide hedging positions in equivalent core referenced futures contract units, excluding all or part of the commodity that it excludes in its regular business practice. The commenter also suggested that if the filer is cross hedging, the filer must also report the aggregated quantity of bona fide hedge positions it is cross hedging in terms of the actual commodity as well as specify the futures market in which it is hedging.[930]

Another commenter suggested that the information required on Form 204 is ''ambiguous'' and asked the Commission to clarify what scope of, for example, stocks or fixed price purchase and sales agreements must be reported as well as what level of data precision is required.[931]

A commenter requested that the Commission allow hedges to be reported on a ''macro'' basis (*e.g.* futures positions vs. cash positions) as opposed to requiring the matching of individual physical market transactions to enumerated bona fide hedges. The commenter stated that performing specific linkage of individual physical transactions to individual hedge transactions is burdensome and does not provide any ''managerial or economic benefit.'' [932]

In contrast, another commenter suggested that the Commission tailor the series '04 reports to require ''only the information that is required to justify the claimed hedge exemption.'' The commenter stated that Form 204 appears to require a market participant to list all cash market exposures, even if the exposures are not relevant to the bona fide hedge exemption being claimed, which it believes would provide no value to the Commission in determining whether a hedge was bona fide.[933]

Another commenter stated that because the prompt (spot) month for certain referenced contracts will no longer trade as of the last Friday of the month, a market participant that exceeds a spot-month position limit who no longer has that spot-month position should not be required to report futures-equivalent positions for referenced contract on Form 204.[934] The commenter recommended that the Commission should require a market

[929] The Commission notes that Form 704 has been removed from the list of series '04 forms that could be required under a special call. This is a non-substantive change resulting from changes made to § 150.7, discussed *infra.*

[930] CL–Working Group–60947 at 17–18.

[931] CL–COPE–60932 at 10. The commenter made the same requests for clarification regarding the cash market information required on Form 504; since the information is similar, the Commission is responding here to the comment for both forms.

[932] CL–ASR–60933 at 5.

[933] *See* CL–Working Group–60396 at 17.

[934] CL–FIA–59595 at 37–38.

participant with a position in excess of a spot-month position limit to report on Form 204 only the cash-market activity related to that particular spot-month derivative position, and not to require it to report cash-market activity related to non-spot-month positions where it did not exceed a non-spot-month position limit; the commenter stated that the burden associated with such a reporting obligation would increase significantly.[935] Separately, another commenter claimed that Form 204 appears to address only non-spot-month position limits and asked the Commission to clarify how it will distinguish reporting on Form 204 that is related to a spot-month position limit versus a non-spot-month position limit.[936]

One commenter recommended that reporting rules require traders to identify the specific risk being hedged at the time a trade is initiated, to maintain records of termination or unwinding of a hedge when the underlying risk has been sold or otherwise resolved, and to create a practical audit trail for individual trades, to discourage traders from attempting to mask speculative trades under the guise of hedges.[937]

*Commission Reproposal:* In response to the modifications to Form 204 proposed by the commenter, the Commission notes that no modifications are necessary because the form, as proposed, requires the reporting of aggregated quantity of cash positions that underlie bona fide hedging positions in equivalent core referenced futures contract units, excluding a de minimis portion of the commodity, products, and byproducts that it excludes in its regular business practice.[938] Reproposed Form 204 also requires cross-hedgers to report the aggregated quantity of bona fide hedging positions it is cross hedging in terms of the actual commodity as well as specify the futures market in which it is hedging.

The Commission reproposes that the Form 204 requires a market participant to report all cash market positions in any commodity in which the participant has exceeded a spot-month or non-spot-month position limit. Form 204 is not intended to match a firm's hedged positions to underlying cash positions on a one-to-one basis; rather, it is intended to provide a ''snapshot'' into the firm's cash market position in a particular commodity as of one day during a month. The information on this form is used for several purposes in addition to reviewing hedged positions, including helping Surveillance analysts understand changes in the market fundamentals in underlying commodity markets.[939] The Commission believes that adopting the commenters' recommendations to require cash market information underlying a single derivative hedge position would result in a more burdensome reporting process for firms, particularly those who hedge on a portfolio basis. Instead, the Commission is confirming that, as requested by the commenter, cash market positions should be reported on an aggregated or ''macro'' basis.

The Commission notes that this ''snapshot'' requirement has historically been—and is currently—required on Form 204 for the nine legacy agricultural contracts. Further, the Commission understands that exchange hedge application forms require similar cash position information; firms that have applied to an exchange for hedge exemptions in non-legacy contracts should already be familiar with providing cash market information when they exceed a position limit or a position accountability level.

The commenters that focus on the Form 204 as it relates to exceeding either spot-month position limits or non-spot-month position limits contrast each other: one believed Form 204 was to be filed in response to exceeding only spot-month position limits and the other that Form 204 was to be filed in response to exceeding only non-spot-month position limits. However, the Commission has never distinguished between spot-month limits and non-spot-month limits with respect to the filing of Form 204. The Commission notes that, as discussed in the December 2013 Position Limits Proposal, Form 204 is used to review positions that exceed speculative limits in general, not just in the spot-month.[940] Because of this, the Commission is not adopting the commenter's recommendation to only require Form 204 when a market participant exceeds a spot-month limit.

In response to the commenter who suggested the Commission require a ''practical audit trail'' for bona fide hedgers, the Commission notes that other sections of the Commission's regulations provide rules regarding detailed individual transaction recordkeeping as suggested by the commenter.

ii. Cotton Merchants and Dealers Reporting on Form 304—§ 19.02

*Proposed Rule:* In the December 2013 Position Limits Proposal, the Commission proposed to continue to require the filing of Form 304, which requires information on the quantity of call cotton bought or sold, on a weekly basis. The Commission noted that Form 304 is required in order for the Commission to produce its weekly cotton ''on call'' report.[941] The Commission also proposed to relocate the list of required information for Form 304 from current § 19.01(a) to proposed § 19.01(a)(3).

*Comments Received:* The Commission did not receive any comments on the proposed changes to Form 304.

*Commission Reproposal:* The Commission is reproposing Form 304, as originally proposed.

iii. Conditional Spot-Month Limit Exemption Reporting on Form 504—§ 19.01(a)(1)

*Proposed Rule:* As proposed, § 19.01(a)(1) would require persons availing themselves of the conditional spot-month limit exemption (pursuant to proposed § 150.3(c)) to report certain detailed information concerning their cash market activities for any commodity specially designated by the Commission for reporting under § 19.03 of this part. In the December 2013 Position Limits Proposal, the Commission noted its concern about the cash market trading of those availing themselves of the conditional spot-month limit exemption and so proposed to require that persons claiming a conditional spot-month limit exemption must report on new Form 504 daily, by 9 a.m. Eastern Time on the next business day, for each day that a person is over the spot-month limit in certain

[935] CL–FIA–59595 at 38.

[936] CL–ASR–60933 at 4.

[937] CL–Sen. Levin–59637 at 8.

[938] *See* supra discussion of the exclusion of certain source commodities, products, and byproducts of the cash commodity hedged when reporting on Form 204.

[939] In the December 2013 Position Limits Proposal, the Commission highlighted the importance of the data collected on Form 204 to its Surveillance program, stating that ''[c]ollection of this information would facilitate the Commission's surveillance program with respect to detecting and deterring trading activity that may tend to cause sudden or unreasonable fluctuations or unwarranted changes in the prices of the referenced contracts and their underlying commodities.'' *See* December 2013 Position Limits Proposal, 78 FR at 75742.

[940] The Commission stated that the Form 204 ''must show the trader's positions in the cash market and are used by the Commission to determine whether a trader has sufficient cash positions that justify futures and option positions above the speculative limits'' because the Commission is seeking to ''ensure that any person who claims any exemption from federal speculative position limits can demonstrate a legitimate purpose for doing so.'' *See* December 2013 Position Limits Proposal, 78 FR at 75741–2.

[941] The Commission's Weekly Cotton On-Call Report can be found here: *http://www.cftc.gov/MarketReports/CottonOnCall/index.htm.*

special commodity contracts specified by the Commission.

The Commission proposed to require reporting on new Form 504 for conditional spot-month limit exemptions in the natural gas commodity derivative contracts only.

*Comments Received:* One commenter stated its belief that the information required on Form 504 is redundant of information required on Form 204 and would overly burden hedgers.[942] The commenter suggested that, if the Commission decides to retain the conditional spot-month limit exemption, and thereby Form 504, the Commission should require only an affirmative representation from market participants that they do not hold any physical delivery Referenced Contracts.[943]

Another commenter stated that Form 504 creates a burden for hedgers to track their cash business and affected contracts and to create systems to file multiple forms. The commenter noted its belief that end-users/hedgers should never be subjected to the daily filing of reports.[944] Further, the commenter suggested the Commission delete Form 504 entirely, asserting that it will be unnecessary if the Commission adopts the commenter's separate cash settled limit idea (the commenter proposed a higher cash settled limit with no condition on the physical delivery market).[945] Another commenter suggested deleting the Form 504 because it believes that no matter how extensive the Commission makes reporting requirements, the Commission will still need to request additional information on a case-by-case basis to ensure hedge transactions are legitimate.[946]

A third commenter suggested that the Commission should modify the data requirements for Form 504 in a manner similar to the approach used by ICE Futures U.S. for natural gas contracts, that is, requiring a description of a market participant's cash-market positions as of a specified date filed in advance of the spot-month.[947]

*Commission Reproposal:* The Commission has tentatively determined under § 19.03 to designate the Henry Hub Natural Gas referenced contracts for reporting of a conditional spot-month limit exemption under § 19.00(a)(1)(i).

In response to the first three commenters, the Commission reiterates a key distinction between the Form 504 and the Form 204. Form 504 is required of speculators that are relying upon the conditional spot-month limit exemption. Form 204 is required for hedgers that exceed position limits. To the extent a firm is hedging, there is no requirement to file the Form 504.

In the unlikely event that a firm is both hedging and relying upon the conditional spot-month limit exemption, the firm would be required to file both forms at most one day a month, given the timing of the spot-month in natural gas markets (the only market for which Form 504 will be required at first). In that event, however, the Commission believes that requiring similar information on both forms should encourage filing efficiencies rather than duplicating the burden. For example, both forms require the filer to identify fixed price purchase commitments; the Commission believes it is not overly burdensome for the same firm to report such similar information on the Form 204 and the Form 504, should a market participant ever be required to file both forms.

The Commission is not adopting the commenters' recommendations to delete the Form 504 or to require only an affirmative representation that the condition of the conditional spot-month limit exemption has been met (*i.e.* that the trader holds no position in physical delivery referenced contracts). The Commission explained in the December 2013 Position Limits Proposal that its primary motive in requiring the cash market information required on Form 504 is the need to detect and deter manipulative activities in the underlying cash commodity that might be used to benefit a derivatives position (or vice-versa).[948]

In response to the third commenter, the Commission does not believe that a description of a cash market position is sufficient to allow Commission staff to administer its Surveillance program. Descriptions are not as exact as reported information, and the Commission believes the information gathered in daily Form 504 reports would be more complete—and thus more beneficial—in determining compliance and detecting and deterring manipulation.

The Commission notes that since the Commission is proposing to limit the conditional spot month limit exemption to natural gas markets, the Form 504 will only be required from participants in natural gas markets who seek to avail themselves of the conditional spot-month limit exemption and any corresponding burden will apply to only those participants.

iv. Pass-Through Swap Exemption Reporting on Form 604—§ 19.01(a)(2)

*Proposed Rule:* As proposed, § 19.01(a)(2) would require a person relying on the pass-through swap exemption who holds either of two position types to file a report with the Commission on new Form 604.[949] The first type of position, filed on Section A of Form 604, is a swap executed opposite a bona fide hedger that is not a referenced contract and for which the risk is offset with referenced contracts (*e.g.,* cross commodity hedging positions). The second type of position, filed on Section B of Form 604, is a cash-settled swap (whether or not the swap is, itself, a referenced contract) executed opposite a bona fide hedger that is offset with physical-delivery referenced contracts held into a spot-month.

These reports on Form 604 would explain hedgers' needs for large referenced contract positions and would give the Commission the ability to verify the positions were a bona fide hedge, with heightened daily surveillance of spot-month offsets. Persons holding any type of pass-through swap position other than the two described above would report on Form 204.[950]

*Comments Received:* The Commission received three comments regarding Form 604, all from the same commenter. These comments and the Commission's responses are detailed below.

*Comment:* One commenter recommended that the Commission remove the requirement in Form 604 to submit futures-equivalent derivative

[942] CL–Working Group–59693 at 65–66.

[943] CL–Working Group–59693 at 65–66.

[944] CL–COPE–59662 at 24.

[945] CL–COPE–59662 at 24.

[946] CL–NGFA–60941 at 7–8.

[947] CL–FIA–59595 at 37.

[948] Specifically, the Commission stated that ''[w]hile traders who avail themselves of this exemption could not directly influence particular settlement prices by trading in the physical-delivery referenced contract, the Commission remains concerned about such traders' activities in the underlying cash commodity.'' *See* December 2013 Position Limits Proposal, 78 FR at 75744.

[949] Under the definition of bona fide hedging position in Section 4a(c)(2) of the Act, a person who uses a swap to reduce risks attendant to a position that qualifies as a bona fide hedging position may pass-through those bona fides to the counterparty, even if the person's swap position is not in excess of a position limit. As such, positions in commodity derivative contracts that reduce the risk of pass-through swaps would qualify as bona fide hedging positions. *See supra* discussion of the proposed definition of bona fide hedging position.

[950] Persons holding pass-through swap positions that are offset with referenced contracts outside the spot month (whether such contracts are for physical delivery or are cash-settled) need not report on Form 604 because swap positions that are referenced contracts will be netted with offsetting referenced contract positions outside the spot month pursuant to proposed § 150.2(b).

positions, claiming that the Commission did not explain why it needs to obtain data on a market participant's futures-equivalent position as part of proposed Form 604 in light of the commenter's presumption that the Commission already has a market participant's future-equivalent position from large-trader reporting rules and access to SDR data.[951]

*Commission Reproposal:* In response to the commenter, the Commission notes that futures-equivalent position information is necessary to allow staff to match the offset futures position with the non-referenced-contract swap position underlying the hedge because such positions are not subject to part 20 reporting. The Commission notes that Form 604 is filed outside of the spot month only if the swap position being offset is not a referenced contract. Since only referenced contracts are automatically netted for purposes of determining compliance with position limits, the Commission would not have knowledge or reason to net a pass-through swap position with the participant's futures positions without the filing of Form 604. During the spot month, the Commission notes that, while it has access to referenced contract swap positions in part 20 data, the Commission would not know that a particular swap forms the basis for a pass-through swap offset exemption, and so again would not have knowledge or reason to net a pass-through swap position with the participant's futures position. Without Section B of Form 604 filed during the spot month, the Commission may believe a firm is in violation of physical-delivery spot month limits despite the firm being eligible for a pass-through swap offset exemption. The Commission is proposing to require the identification of a particular swap position and the offsetting referenced contract position to alleviate concerns about the disruption of the price discovery function of the underlying physical-delivery contract during the spot month period.

*Comment:* The same commenter also noted that the spot-month for certain referenced contracts will no longer trade as of the last Friday of the month and so recommended that a market participant exceeding a spot-month position limit who no longer has that spot-month position should not be required to report futures-equivalent derivatives positions for referenced contract on Form 604.[952]

*Commission Reproposal:* As proposed, pass-through swap offsets that last into the spot-month would be filed daily during the spot period, not as of the last Friday of the month.[953] Pass-through swap offset positions outside of the spot-month are required to be filed as of the last Friday of the month. The Commission expects that, in most cases, the Form 604 would be filed outside of the spot-month which means only Section A would need to be filed. That filing is required as of the last Friday of the month, the same timeline that is required for the Form 204, for convenience and ease of filing.

*Comment:* Finally, the commenter recommended that CFTC require a market participant with a position in excess of a spot-month position limit to report on Form 604 only the cash-market activity related to that particular spot-month derivative position, and not to require it to report cash-market activity related to non-spot-month positions where it did not exceed a non-spot-month position limit, since the burden associated with such a reporting obligation would increase significantly.[954]

*Commission Reproposal:* The Commission notes in response to the commenter that neither Sections A nor B of Form 604 would require the filer to report cash market activity.

This commenter makes the same remarks regarding Form 204, but the Form 204 requires cash-market activity in a particular commodity whereas the Form 604 requires information on a particular swap market position.

The Commission is reproposing Form 604, as originally proposed.

e. Time and Place of Filing Reports—§ 19.01(b)

*Proposed Rule:* As proposed, § 19.01(b)(1) would require all reports except those submitted in response to special calls or on Form 504, Form 604 during the spot-month, or Form 704 to be filed monthly as of the close of business on the last Friday of the month and not later than 9 a.m. Eastern Time on the third business day following the last Friday of the month.[955] For reports submitted on Form 504 and Form 604 during the spot-month, proposed § 19.01(b)(2) would require filings to be submitted as of the close of business for each day the person exceeds the limit during the spot period and not later than 9 a.m. Easter Time on the next business day following the date of the report.[956] Finally, proposed § 19.01(b)(3) would require series '04 reports to be transmitted using the format, coding structure, and electronic data transmission procedures approved in writing by the Commission or its designee.

*Comments Received:* One commenter stated its support for the proposed monthly, rather than daily, filing of Form 204.[957] Another commenter recommended an annual Form 204 filing requirement, rather than a monthly filing requirement. The commenter noted that because the general size and nature of its business is relatively constant, the differences between each monthly report would be insignificant. The commenter recommended the CFTC ''not impose additional costs of monthly reporting without a demonstration of significant additional regulatory benefits.'' The commenter noted its futures position typically exceeds the proposed position limits, but such positions are bona fide hedging positions. In addition to futures, the commenter noted it executes a small notional volume of swaps as hedges of forward contracts.[958]

Similarly, another commenter suggested that if the Commission does not eliminate the forms in favor of the requirements in the 2016 Supplemental Position Limits Proposal the Commission should require only an annual notice that details its maximum cash market exposure that justifies an exemption, to be filed with the exchange.[959]

One commenter suggested that the reporting date for Form 204 should be the close of business on the day prior to the beginning of the spot period and that it should be required to filed no later than the 15th day of the month following a month in which a filer exceeded a federal limit to allow the market participant sufficient time to collect and report its information.[960]

With regards to proposed § 19.01(b)(2), one commenter recommended CFTC change the proposed next-day reporting of Form 504 for the conditional spot-month limit exemption and Form 604 for the pass-through swap offsets during the spot-month, to a monthly basis, noting

[951] CL–FIA–59595 at 37.

[952] CL–FIA–59595 at 37–38.

[953] *See supra* discussion regarding the time and place of filing series '04 reports.

[954] CL–FIA–59595 at 38.

[955] The timeframe for filing Form 704 is included as part of proposed § 150.7. *See supra* for discussion regarding the filing of Form 704.

[956] In proposed § 19.01(b)(2), the Commission inadvertently failed to include reports filed under § 19.00(a)(1)(ii)(B) *(i.e.* Form 604 during the spot month) in the same filing timeframe as reports filed under § 19.00(a)(1)(i) (*i.e.* Form 504). The correct filing timeframe was described in multiple places on the forms published in the **Federal Register** as part of the December 2013 Position Limits Proposal.

[957] CL–Working Group–59693 at 65.

[958] CL–DFA–59621 at 2.

[959] CL–FIA–60937 at 17.

[960] CL–Working Group–60947 at 17–18.

market participants need time to generate and collect data and verify the accuracy of the reported data. The commenter further stated that CFTC did not explain why it needs the data on Form 504 or Form 604 on a next-day basis.[961]

Another asserted that the daily filing requirement (Form 504) for participants who rely on the conditional spot-month limit exemption ''imposes significant burdens and substantial costs on market participants.'' The commenter urged a monthly rather than a daily filing of all cash market positions, which the commenter claimed is consistent with current exchange practices.[962]

*Commission Reproposal:* The Commission is reproposing § 19.01(b)(1), as originally proposed, with some minor clarifications to the language to make the text easier to follow. As discussed above, the Commission believes that Form 204 provides a monthly ''snapshot'' of the cash market positions of traders whose positions are in excess of spot-month or non-spot-month speculative position limits and for that reason it is necessary to provide its Surveillance program the ability to detect and deter market manipulation and protect the price discovery process. The Commission is retaining the last Friday of the month as the required reporting date in order to avoid confusion and uncertainty, particularly for those participants who already file Form 204 and thus are accustomed to that reporting date.

In response to the commenters' suggestions that Form 204 be filed annually, the Commission notes that throughout the course of a year, most commodities subject to federal position limits under proposed § 150.2 are subject to seasonality of prices as well as less predictable imbalances in supply and demand such that an annual filing would not provide Surveillance insight into cash market trends underlying changes in the derivative markets. This insight is necessary for Surveillance to determine whether price changes in derivative markets are caused by fundamental factors or manipulative behavior. Further, the Commission believes that an annual filing could actually be more burdensome for firms, as an annual filing could lead to special calls or requests between filings for additional information in order for the Commission's Surveillance program to fulfill its responsibility to detect and deter market manipulation. In addition, the Commission notes that while one participant's positions may remain constant throughout a year, the same is not true for many other market participants. The Commission believes that varying the filing arrangement depending on a particular market or market participant is impractical and would lead to increased burdens for market participants due to uncertainty regarding when each firm, or each firm by each commodity, is supposed to file.

The Commission is reproposing, as originally proposed, the provision in proposed § 19.01(b)(2) to require next-day, daily filing of Forms 504 and 604 in the spot-month. In response to the commenter, the Commission notes that it described its rationale for requiring Forms 504 and 604 daily during the spot-month in the December 2013 Position Limits Proposal.[963] In order to detect and deter manipulation during the spot-month, concurrent information regarding the cash positions of a speculator holding a conditional spot-month limit exemption (Form 504) or the swap contract underlying a large offsetting position in the physical delivery contract (Form 604) is necessary during the spot-month. Receiving Forms 504 or 604 before or after the spot-month period would not help the Surveillance program to protect the price discovery process of physical-delivery contracts and to ensure that market participants have a qualifying pass-through swap contract position underlying offsetting futures positions held during the spot-month.

The Commission notes that, as reproposed, the Form 504 is required only for the Natural Gas commodity, which has a 3-day spot period.[964] Daily reporting of the Form 504 during the spot-month allows Surveillance to monitor a market participant's cash market activity that could impact or benefit their derivatives position. Given the short filing period for natural gas and the importance of accurate information during the spot-month, the Commission believes that requiring the Form 504 to be filed daily provides an important benefit that outweighs the potential burdens for filers

As a practical matter, the Commission notes that the Form 604 is collected during the spot-month only under particular circumstances, *i.e.* for an offsetting position in physical delivery referenced contracts during the spot-month. Because the ''five-day rule'' applies to such positions, the spot-month filing of the Form 604 would only occur in contracts whose spot-month period is longer than 5 days (excluding, for example, energy contracts but including many agricultural commodities).[965]

The Commission is reproposing §§ 19.01(b)(1)–(2), as originally proposed, with some minor clarifications to the language to make the text easier to follow. The Commission inadvertently left out of proposed § 19.01(b)(2) a reference to the requirement to file Section B of Form 604 (pass-through swap offsets held into the spot-month). No commenter appeared to be confused about this requirement, as the correct timeframe was described in multiple places on the forms published in the **Federal Register** as part of the December 2013 Position Limits Proposal, but to avoid future confusion the Commission has modified the language—but not the substance—of § 19.01(b)(1)–(2) to clarify the time and place for filing series '04 reports.

Finally, the Commission is reproposing the electronic filing requirement, as originally proposed.[966] Further instructions on submitting '04 reports will be available at *http://www.cftc.gov/Forms/index.htm.*

### *F. § 150.7—Reporting Requirements for Anticipatory Hedging Positions*

#### 1. Reporting Requirements for Anticipatory Hedging Positions and New Form 704

*Proposed Rule:* The Commission's revised definition of bona fide hedging in § 150.1 enumerates two new types of anticipatory bona hedging positions. Two existing types of anticipatory hedges are being continued from the existing definition of bona fide hedging in current § 1.3(z): Hedges of unfilled anticipated requirements and hedges of

[961] CL–FIA–59595 at 35.

[962] CL–ICE–59669 at 7.

[963] December 2013 Position Limits Proposal, 78 FR at 75744–5. The Commission noted that its experience overseeing the ''dramatic instances of disruptive trading practices in the natural gas markets'' warranted enhanced reporting for that commodity during the spot month on Form 504. The Commission noted its intent to wait until it gained additional experience with limits in other commodities before imposing enhanced reporting requirements for those commodities. The Commission further noted that it was concerned that a trader could hold an extraordinarily large position early in the spot month in the physical-delivery contract along with an offsetting short position in a cash-settled contract (such as a swap), and that such a large position could disrupt the price discovery function of the core referenced futures contract.

[964] Reproposed § 150.3(c) provides a conditional spot-month limit exemption only for the natural gas cash-settled referenced contracts.

[965] It should be noted, however that an exchange, using its discretion, could require the filing of Form 604, for example, in an energy contract, as part of the exchange's recognition of a non-enumerated bona fide hedging position under § 150.9, discussed below.

[966] The Commission notes that the electronic filing requirement was proposed in § 19.01(b)(3) but due to other changes within that section it is now located in § 19.01(b)(4). The substance of the requirement has not changed.

unsold anticipated production, as well as anticipatory cross-commodity hedges of such requirements or production.[967] The revised § 150.1 definition expands the list of enumerated anticipatory bona fide hedging positions to include hedges of anticipated royalties and hedges of anticipated services contract payments or receipts, as well as anticipatory cross-commodity hedges of such contracts.[968] As discussed above, § 1.48 has long required special reporting for hedges of unfilled anticipated requirements and hedges of unsold anticipated production because the Commission remains concerned about distinguishing between anticipatory reduction of risk and speculation. Such concerns apply equally to any position undertaken to reduce the risk of anticipated transactions. Hence, the Commission proposed to extend the special reporting requirements in proposed § 150.7 for all types of enumerated anticipatory hedges that appear in the definition of bona fide hedging positions in proposed § 150.1.

The Commission proposed to add a new series '04 reporting form, Form 704, to effectuate these additional and updated reporting requirements for anticipatory hedges. Persons wishing to avail themselves of an exemption for any of the anticipatory hedging transactions enumerated in the updated definition of bona fide hedging in § 150.1 are required to file an initial statement on Form 704 with the Commission at least ten days in advance of the date that such positions would be in excess of limits established in proposed § 150.2. Advance notice of a trader's intended maximum position in commodity derivative contracts to offset anticipatory risks allows the Commission to review a proposed position before a trader exceeds the position limits and, thereby, allows the Commission to prevent excessive speculation in the event that a trader were to misconstrue the purpose of these limited exemptions.[969] The trader's initial statement on Form 704 provides a detailed description of the person's anticipated activity (*i.e.,* unfilled anticipated requirements, unsold anticipated production, etc.).[970] Under proposed § 150.7(b), the Commission may reject all or a portion of the position as not meeting the requirements for bona fide hedging positions under proposed § 150.1. To support this determination, proposed § 150.7(c) would allow the Commission to request additional specific information concerning the anticipated transaction to be hedged. Otherwise, Form 704 filings that conform to the requirements set forth in § 150.7 would become effective ten days after submission. As proposed, § 150.7(e) would require an anticipatory hedger to file a supplemental report on Form 704 whenever the anticipatory hedging needs increase beyond that in its most recent filing.

As proposed, § 150.7(f) would add a requirement for any person who files an initial statement on Form 704 to provide annual updates that detail the person's actual cash market activities related to the anticipated exemption. With an eye towards distinguishing bona fide hedging of anticipatory risks from speculation, annual reporting of actual cash market activities and estimates of remaining unused anticipated exemptions beyond the past year would enable the Commission to verify whether the person's anticipated cash market transactions closely track that person's real cash market activities. In addition, § 150.7(g) would enable the Commission to review and compare the actual cash activities and the remaining unused anticipated hedge transactions by requiring monthly reporting on Form 204. Absent monthly filing, the Commission would need to issue a special call to determine why a person's commodity derivative contract position is, for example, larger than the pro rata balance of her annually reported anticipated production.

As is the case under current § 1.48, § 150.7(h) requires that a trader's maximum sales and purchases must not exceed the lesser of the approved exemption amount or the trader's current actual anticipated transaction.

For purposes of simplicity, the special reporting requirements for anticipatory hedges are located within the Commission's position limits regime in part 150, and alongside the Commission's updated definition of bona fide hedging positions in § 150.1. Thus, the Commission is proposing to delete the reporting requirements for anticipatory hedges in current § 1.48 because that section would be duplicative.

*Comments Received:* One commenter asserted that the reporting requirements for anticipatory hedges of an operational or commercial risk comprising an initial, supplementary and annual report are unduly burdensome. The commenter recommended that the Commission require either an initial and annual report or an initial and supplementary report.[971]

Another commenter suggested deleting the Form 704 because it believes that no matter how extensive the Commission makes reporting requirements, the Commission will still need to request additional information on a case-by-case basis to ensure hedge transactions are legitimate.[972] The commenter suggested that the Commission should be able to achieve its goal of obtaining enough information to determine whether to request additional information using the Form 204 along with currently collected data sources and so the additional burden of the new series '04 reports outweighs the benefit to the Commission.[973]

Several commenters remarked on the cost associated with the proposed Form 704. One commenter stated that the additional reporting requirements, including new Form 704 to replace the reporting requirements under current rule 1.48, and annual and monthly reporting requirements under proposed rules 150.7(f) and 150.7(g) ''will impose significant additional regulatory and compliance burdens on commercials and believes that the Commission should consider alternatives, including targeted special calls when appropriate.'' [974] Another commenter stated the reporting requirements for the series 04 forms is overly burdensome and would impose a substantial cost to market participants because while the proposal would require the Commission to respond fairly quickly, it does not provide an indication of whether the Commission will deem the requirement accepted if the Commission doesn't respond within a time frame. The commenter is concerned that a market participant may have to refuse business if it does not receive an approved exemption in advance of a transaction.[975] A third commenter stated that Form 704 is ''commercially impracticable and unduly burdensome'' because it would require filers to

[967] *See* current definition of bona fide hedging transactions at 17 CFR 1.3(z)(2)(i)(B) and (ii)(C), respectively. Cross-commodity hedges are permitted under 17 CFR 1.3(z)(2)(iv). *Compare with* paragraphs (3)(iii) and (4)(i), respectively, of the definition of bona fide hedging positions in proposed § 150.1, discussed *above.*

[968] *See* sections (4)(iii), (4)(iv), and (5), respectively, of the definition of bona fide hedging positions in § 150.1, discussed *above.*

[969] Further, advance filing may serve to reduce the burden on a person who exceeds position limits and who may then otherwise be issued a special call to determine whether the underlying requirements for the exemption have been met. If the Commission were to reject such an exemption, such a person would have already violated position limits.

[970] Proposed 150.7(d)(2) would require additional information for cross hedges, for reasons discussed above.

[971] CL–IECAssn–59679 at 11.

[972] CL–NGFA–60941 at 7–8.

[973] *Id.*

[974] CL–APGA–59722 at 10.

[975] CL–EDF–59961 at 6.

''analyze each transaction to see if it fits into an enumerated hedge category.'' The commenter is concerned that such ''piecemeal review'' would require a legal memorandum and the development of new software to track positions and, since the Commission proposed that Form 704 to be used in proposed § 150.11, the burden associated with the form has increased.[976]

One commenter highlighted discrepancies between the instructions for Form 704 and the data on the sample Form 704. The commenter noted that instructions for column five request the ''Cash commodity same as (S) or cross-hedged (C–H) with Core Reference Futures Contract (CFRC)'' while the sample Form 704 lists ''CL–NYMEX'' as the information reported in that column. The commenter also noted that Form 704 has eleven columns, while the sample Form 704 contains only ten columns, omitting a column for ''Core Referenced Futures contract (CRFC).''[977]

The commenter also requested that the Commission clarify instructions for column six of proposed Form 704 to permit a reasonable estimate of anticipated production (or other anticipatory hedge) based on commercial experience, in the event the market participant does not have three years of data related to the anticipated hedge, for example, of anticipated production of a newly developed well.[978]

*Commission Reproposal:* As discussed in the December 2013 Position Limits Proposal, the Commission remains concerned about distinguishing between anticipatory reduction of risk and speculation.[979] Therefore, the Commission is again proposing the requirement to file Form 704 for anticipatory hedges. The Commission notes that most of the information required on Form 704 is currently required under § 1.48, and that such information is not found in any other Commission data source, including Form 204.

The Commission is proposing several changes to § 150.7 in order to make the requirements for Form 704 clearer and more concise. For example, the Commission is adopting the commenter's suggestion to require the initial statement and annual update but eliminate the supplemental filing as proposed in § 150.7(e). Current § 1.48 contains a requirement for supplemental filings similar to proposed § 150.7(e), but unlike current § 1.48, the proposed rules also require monthly reporting on Form 204 and annual updates to the initial statement. After considering the commenter's concerns, the Commission believe the monthly reporting on Form 204 and annual updates on Form 704 will provide sufficient updates to the initial statement and is deleting the supplemental filing provision in proposed § 150.7(e) to reduce the burden on filers as suggested by the commenter.

In addition, the Commission is combining the list of required information on Form 704 into one section, since such information is almost identical for the initial statement and the required annual updates. In this Reproposal, two nearly identical lists of information have been combined into one list in § 150.7(d). This reorganization is intended to make compliance with § 150.7, including the filing of Form 704, simpler and easier to understand for market participants. Changes have been made throughout part 19 and part 150 to conform to the deletion of the required supplemental filing and the reorganization of § 150.7. In particular, the Commission altered § 19.01(a)(4) to reflect the deletion of the supplemental update and to clarify that persons required to file series '04 reports under § 19.00(a)(1)(iv) must file only Form 204 as required in § 150.7(e).

Finally, the sample Form 704 found in Appendix A to part 19 has also been updated to reflect the combination of the initial statement and annual update into one section. Specifically, on proposed Form 704 had two sections: Section A required information regarding the initial statement and supplemental updates and Section B was required for annual updates. Due to the above-mentioned changes, Section B has been deleted and Section A has been re-labeled as requiring information regarding both the initial statement and the annual update. In order to differentiate between a firm's initial statement and its annual updates regarding the same, the Commission has added a check-box field that requires traders to identify whether they are filing Form 704 to submit an initial statement or to file the required annual update. The Commission believes the addition of this field poses no significant additional burden; rather, the Commission believes the changes to the form, as discussed above, reduce burden to a far greater extent than a minor addition of a check box adds burden.

In response to the commenter who suggested the Commission consider target special calls and other alternatives to the annual and monthly filings, the Commission believes these filings are critical to the Commission's Surveillance program. Anticipatory hedges, because they are by definition forward-looking, require additional detail regarding the firm's commercial practices in order to ensure that a firm is not using the provisions in proposed § 150.7 to evade position limits. In contrast, special calls are backward-looking and would not provide the Commission's Surveillance program with the information needed to prevent markets from being susceptible to excessive speculation. However, the Commission expects the new filing requirements to be an improvement over current practice under § 1.48 because as facts and circumstances change, Surveillance will have a more timely understanding of the market participant's hedging needs.

The Commission notes in response to the commenter that Form 704 is filed in anticipation of risk to be assumed at a future date; market participants will need to provide a detailed description of anticipated activity but there is no requirement to analyze individual transactions or submit a memorandum.

The Commission also notes that concerns regarding a firm having to decline business, because an exemption has not been approved, are unwarranted. Series '04 reports (other than the initial statement of Form 704) are self-effectuating and do not require Commission notification to become effective. With respect to Form 704, the Commission explained in the December 2013 Position Limits Proposal that if the Commission does not notify a market participant within the timeframe indicated in § 150.7(b), the filing becomes effective automatically.[980]

The commenter is correct in noting that there is an error on the Sample Form 704 such that column five (''Core Referenced Futures Contract (CRFC)'') was inadvertently omitted from the Sample Form provided in the proposed rules. The Commission is amending the Sample Form 704 in the reproposed rules to ensure it accurately reflects the requirements of the Form 704 as described in § 150.7(d). Further, the Commission is deleting the condition that requires the specified operating

[976] CL–EEI–EPSA–60925 at 9.

[977] CL–FIA–59595 at 39.

[978] CL–FIA–59595 at 39.

[979] *See* December 2013 Position Limits Proposal, 78 FR at 75746.

[980] *See* the December 2013 Position Limits Proposal, 78 FR at 75746: ''Under proposed § 150.7(b), the Commission may reject all or a portion of the position as not meeting the requirements for bona fide hedging positions under § 150.1. . . . Otherwise, Form 704 filings that conform to the requirements set forth in proposed § 150.7 would become effective ten days after submission.''

period may not exceed one year for agricultural commodities, as end-users in certain agricultural commodities may hedge their positions several years out along the curve.

The Commission notes, in response to the commenter's concern regarding column 6 of Form 704, that the requirement to file the past three years of annual production is also in current § 1.48. Understanding the recent history of a firm's production is necessary to ensure the requested anticipated hedging amount is reasonable. However, the Commission notes that it may permit a reasonable, supported estimate of anticipated production for less than three years of annual production data, in the Commission's discretion, if a market participant does not have three years of data. The Commission is amending the form instructions to clarify that Commission staff could determine that such an estimate is reasonable and so would be accepted.

Finally, the Commission notes that several references to other provisions within part 150 contained in §§ 150.7(b), 150.7(d), and 150.7(h) were incorrectly cited in the December 2013 Position Limits Proposal; the Commission is revising these paragraphs to ensure all references are up-to-date and correct.

2. Delegation

*Proposed Rule:* In § 150.7(i), the Commission proposed to delegate to the Division of Market Oversight director or staff the authority: To provide notice to a firm who has filed Form 704 that they do not meet the requirements for bona fide hedging; to request additional or updated information under § 150.7(c); and to request under § 150.7(d)(2) information concerning the basis for and derivation of conversion factors used in computing the position information provided in Form 704.

*Comments Received:* The Commission received no comments on the proposed delegation of authority under § 150.7.

*Commission Reproposal:* The Commission is reproposing § 150.7(i), as originally proposed.

*G. § 150.9—Process for Recognition of Positions as Non-Enumerated Bona Fide Hedging Positions*

1. Overview of Proposed Rules Related to Recognition of Bona Fide Hedging Positions and Granting of Spread Exemptions

In the 2016 Supplemental Position Limits Proposal, the Commission noted that it was proposing three sets of Commission rules under which an exchange could take action to recognize certain bona fide hedging positions and to grant certain spread exemptions, with regard to both exchange-set and federal position limits.[981] The Commission pointed out that in each case, the proposed rules would establish a formal CFTC review process that would permit the Commission to revoke all such exchange actions.

As the Commission observed at that time, its authority to permit certain exchanges to recognize positions as bona fide hedging positions is found, in part, in CEA section 4a(c)(1), and under CEA section 8a(5), which provides that the Commission may make such rules as, in the judgment of the Commission, are reasonably necessary to effectuate any of the provisions or to accomplish any of the purposes of the CEA. CEA section 4a(c)(1) provides that no CFTC rule applies to ''transaction or positions which are shown to be bona fide hedging transactions or positions,'' as those terms are defined by Commission rule consistent with the purposes of the CEA.[982] The Commission noted that ''shown to be'' is passive voice, which could encompass either a position holder or an exchange being able to ''show'' that a position is entitled to treatment as a bona fide hedging position, and does not specify that the Commission must determine in advance whether the position or transaction was shown to be bona fide. The Commission interpreted CEA section 4a(c)(1) to authorize the Commission to permit certain SROs (*i.e.,* DCMs and SEFs, meeting certain criteria) to recognize positions as bona fide hedging positions for purposes of federal limits, subject to Commission review.

The Commission observed that for decades, exchanges have operated as self-regulatory organizations, and pointed out further that these self-regulatory organizations have been charged with carrying out regulatory functions, including, since 2001, complying with core principles, and operate subject to the regulatory oversight of the Commission pursuant to the CEA as a whole, and more specifically, CEA sections 5 and 5h.[983] In addition, the Commission pointed out that as self-regulatory organizations, exchanges do not act only as independent, private actors;[984] when the Act is read as a whole, as the Commission noted in 1981, ''it is apparent that Congress envisioned cooperative efforts between the self-regulatory organizations and the Commission. Thus, the exchanges, as well as the Commission, have a continuing responsibility in this matter under the Act.''[985] The Commission

[981] *See generally* 2016 Supplemental Position Limits Proposal, 81 FR at 38464–82; the Commission incorporates herein its explanation of its proposed adoption of §§ 150.9, 150.10 and 150.11. Under the proposal, exchanges would be able to: (i) Recognize certain non-enumerated bona fide hedging positions, *i.e.,* positions that are not enumerated by the Commission's rules (pursuant to proposed § 150.9); (ii) grant exemptions to position limits for certain spread positions (pursuant to proposed § 150.10); and (iii) recognize certain enumerated anticipatory bona fide hedging positions (pursuant to proposed § 150.11).

[982] 2016 Supplemental Position Limits Proposal, 81 FR at 38464.

[983] *Id.* at 38465. The Commission noted that CFTC § 1.3(ee) defines SRO to mean a DCM, SEF, or registered futures association (such as the National Futures Association), and also pointed out that under the Commission's regulations, self-regulatory organizations have certain delineated regulatory responsibilities, which are carried out under Commission oversight and which are subject to Commission review. *Id.*

[984] *Id.* The Commission stated that it ''views as instructive'' three examples of case law addressing grants of authority by an agency (the Securities and Exchange Commission, the 'SEC') to a self-regulatory organization ('SRO') (in the SEC cases the SRO was NASD, now FINRA), providing insight into the factors addressed by the court regarding oversight of an SRO;

(i) In 1952, the Second Circuit reviewed an SEC order that failed to set aside a penalty fixed by NASD suspending the defendant broker-dealer from membership. *Citing Sunshine Anthracite Coal Co.* v. *Adkins,* 310 U.S. 381 (1940), the Second Circuit found that, in light of the statutory provisions vesting the SEC with power to approve or disapprove NASD's rules according to reasonably fixed statutory standards, and the fact that NASD disciplinary actions are subject to SEC review, there was 'no merit in the contention that the Maloney Act unconstitutionally delegates power to the NASD.' *R.H. Johnson* v. *Securities and Exchange Commission,* 198 F. 2d 690, 695 (2d Cir. 1952).

(ii) In 1977, the Third Circuit, in *Todd & Co.* v. *Securities and Exchange Commission* ('*Todd*'), 557 F.2d 1008 (3rd Cir. 1977), likewise concluded that the Act did not unconstitutionally delegate legislative power to a private institution. The *Todd* court articulated critical factors that kept the Maloney Act within constitutional bounds. First, the SEC had the power, according to reasonably fixed statutory standards, to approve or disapprove NASD's rules before they could go into effect. Second, all NASD judgments of rule violations or penalty assessments were subject to SEC review. Third, all NASD adjudications were subject to a de novo (non-deferential) standard of review by the SEC, which could be aided by additional evidence, if necessary. *Id.* at 1012. Based on these factors, the court found that '[NASD's] rules and its disciplinary actions were subject to full review by the SEC, a wholly public body, which must base its decision on its own findings' and thus that the statutory scheme was constitutional. *Id.* at 1012–13. *See also First Jersey Securities* v. *Bergen,* 605 F.2d 690 (1979), applying the same three-part test delineated in *Todd,* and then upholding a statutory narrowing of the Todd test.

(iii) In 1982, the Ninth Circuit considered the constitutionality of Congress' delegation to NASD in *Sorrel* v. *Securities and Exchange Commission,* 679 F. 2d 1323 (9th Cir. 1982). *Sorrel* followed *R.H. Johnson, Todd* and *First Jersey* in holding that because the SEC reviews NASD rules according to reasonably fixed standards, and the SEC can review any NASD disciplinary action, the Maloney Act does not impermissibly delegate power to NASD.''

[985] 2016 Supplemental Position Limits Proposal, 81 FR at 38465.

noted that its approach to its oversight of its SROs was subsequently ratified by Congress in 1982, when it gave the CFTC authority to enforce exchange set limits. Further, the Commission observed that as it stated in 2010, ''since 1982, the Act's framework explicitly anticipates the concurrent application of Commission and exchange-set speculative position limits. The Commission further noted that the 'concurrent application of limits is particularly consistent with an exchange's close knowledge of trading activity on that facility and the Commission's greater capacity for monitoring trading and implementing remedial measures across interconnected commodity futures and option markets.' ''[986]

The Commission also noted that under its proposal, it would retain the power to approve or disapprove the rules of exchanges, under standards set out pursuant to the CEA, and to review an exchange's compliance with those rules.[987] Moreover, the Commission observed that it was not diluting its ability to recognize or not recognize bona fide hedging positions or to grant or not grant spread exemptions, as it reserved to itself the ability to review any exchange action, and to review any application by a market participant to an exchange, whether prior to or after disposition of such application by an exchange.

2. Proposed § 150.9—General

*Proposed Rule:* In light of DCM experience in granting non-enumerated bona fide hedging position exemptions to exchange-set position limits for futures contracts, and after consideration of comments recommending exchange review of non-enumerated bona fide hedging position requests, the Commission proposed to permit exchanges to recognize non-enumerated bona fide hedging positions with respect to the proposed federal speculative position limits. Under proposed § 150.9, an exchange, as an SRO[988] that is under Commission oversight and whose rules are subject to Commission review,[989] could establish rules under which the exchange could recognize as non-enumerated bona fide hedging positions, positions that meet the general definition of bona fide hedging position in proposed § 150.1, which implements the statutory directive in CEA section 4a(c) for the general definition of bona fide hedging positions in physical commodities.[990] The exchange's recognition would be subject to review by the Commission. Exchange recognition of a position as a non-enumerated bona fide hedging position would allow the market participant to exceed the federal position limit to the extent that it relied upon the exchange's recognition unless and until such time that the Commission notified the market participant to the contrary.[991] The Commission could issue such a notification in accordance with the proposed review procedures. That is, if a party were to hold positions pursuant to a non-enumerated bona fide hedging position recognition granted by the exchange, such positions would not be subject to federal position limits, unless or until the Commission were to determine that such non-enumerated bona fide hedging position recognition was inconsistent with the CEA or CFTC regulations thereunder. Under this framework, the Commission would continue to exercise its authority in this regard by reviewing an exchange's determination and verifying whether the facts and circumstances in respect of a derivative position satisfy the requirements of the general definition of bona fide hedging position proposed in § 150.1.[992] If the Commission determined that the exchange-granted recognition was inconsistent with section 4a(c) of the Act and the Commission's general definition of bona fide hedging position in § 150.1 and so notified a market participant relying on such recognition, the market participant would be required to reduce the derivative position or otherwise come into compliance with position limits within a commercially reasonable amount of time.

The Commission noted its belief that permitting exchanges to so recognize non-enumerated bona fide hedging positions is consistent with its statutory

[986] *Id.* at 38466.

[987] The Commission stated that ''In connection with recognition of bona fide hedging positions, the Commission notes that the statute is silent or ambiguous with respect to the specific issue—whether the CFTC may authorize SROs to recognize positions as bona fide hedging positions. CEA section 4a(c) provides that no Commission rule establishing federal position limits applies to positions which are shown to be bona fide hedging positions, as such term shall be defined by the CFTC. As noted above, the 'shown to be' phrase is passive voice, which could encompass either a position holder or an exchange being able to ''show'' that a position is entitled to treatment as a bona fide hedge, and does not specify that the Commission must be the party determining in advance whether the position or transaction was shown to be bona fide; the Commission interprets that provision to permit certain SROs (*i.e.,* DCMs and SEFs, meeting certain criteria) to recognize positions as bona fide hedges for purposes of federal limits when done so within a regime where the Commission can review and modify or overturn such determinations. Under the 2016 Position Limits Supplemental Proposal, an SRO's recognition is tentative, because the Commission would reserve the power to review the recognition, subject to the reasonably fixed statutory standards in CEA section 4a(c)(2) (directing the CFTC to define the term bona fide hedging position). An SRO's recognition would also be constrained by the SRO's rules, which would be subject to CFTC review under the proposal. The SROs are parties that are subject to Commission authority, their rules are subject to Commission review and their actions are subject to Commission de novo review under the proposal—SRO rules and actions may be changed by the Commission at any time.'' *Id.*

[988] As noted above, under the Commission's regulations, SROs have certain delineated regulatory responsibilities, which are carried out under Commission oversight and which are subject to Commission review. *See also* 2016 Position Limits Supplemental Proposal, n. 126 (describing reviews of DCMs carried out by the Commission).

[989] *See* CEA section 5c(c), 7 U.S.C. 7a–2(a) (providing Commission with authority to review rules and rule amendments of registered entities, including DCMs).

[990] As previously noted, Congress has required in CEA section 4a(c) that the Commission, within specific parameters, define what constitutes a bona fide hedging position for the purpose of implementing federal position limits on physical commodity derivatives, including, as previously stated, the inclusion in new section 4a(c)(2) of a directive to narrow the bona fide hedging definition for physical commodity positions from that currently in Commission regulation § 1.3(z). *See* 2016 Supplemental Position Limits Proposal, nn. 32 and 105 and accompanying text; *see also* December 2013 Positions Limits Proposal at 75705. In response to that mandate, the Commission proposed in its December 2013 Position Limits Proposal to add a definition of bona fide hedging position in § 150.1, to replace the definition in current § 1.3(z). *See* 78 FR at 75706, 75823.

For the avoidance of doubt, the Commission is still reviewing comments received on these provisions. The Commission is proposing to finalize the general definition of bona fide hedging position based on the standards of CEA section 4a(c), and may further define the bona fide hedging position definition consistent with those standards.

[991] *See generally* the discussion of proposed § 150.9(d) and the requirements regarding the review of applications by the Commission in the 2016 Position Limits Supplemental Proposal. The Commission noted that exchange participation is voluntary, not mandatory and that exchanges could elect not to administer the process. Market participants could still request a staff interpretive letter under § 140.99 or seek exemptive relief under CEA section 4a(a)(7), per the December 2013 Position Limits Proposal. The process does not protect exchanges or applicants from charges of violations of applicable sections of the CEA or other Commission regulations. For instance, a market participant's compliance with position limits or an exemption thereto would not confer any type of safe harbor or good faith defense to a claim that he had engaged in an attempted manipulation, a perfected manipulation or deceptive conduct; *see* the discussion of § 150.6 (Ongoing application of the Act and Commission regulations) as proposed in the December 2013 Position Limits Proposal, 78 FR at 75746–7.

[992] *See* the general discussion of the Commission's review process proposed in § 150.9(d); *see also* the requirement for a weekly report, proposed in § 150.9(c), which would support the Commission's surveillance program by facilitating the tracking of non-enumerated bona fide hedging positions recognized by exchanges, keeping the Commission informed of the manner in which an exchange is administering its procedures for recognizing such non-enumerated bona fide hedging positions.

obligation to set and enforce position limits on physical commodity contracts, because the Commission would be retaining its authority to determine ultimately whether any non-enumerated bona fide hedging positions so recognized is in fact a bona fide hedging position. The Commission's authority to set position limits does not extend to any position that is shown to be a bona fide hedging position.[993] Further, most, if not all, DCMs already have a framework and application process to recognize non-enumerated positions, for purposes of exchange-set limits, as within the meaning of the general bona fide hedging definition in § 1.3(z)(1).[994] The Commission has a long history of overseeing the performance of the DCMs in granting exemptions under current exchange rules regarding exchange-set position limits[995] and believed that it would be efficient and in the best interest of the markets, in light of current resource constraints,[996] to rely on the exchanges to initially process applications for recognition of positions as non-enumerated bona fide hedging positions. In addition, because many market participants are familiar with current DCM practices regarding bona fide hedging positions, permitting DCMs to build on current practice may reduce the burden on market participants. Moreover, the Commission believed that the process outlined in the 2016 Position Limits Supplemental Proposal should reduce duplicative efforts because market participants seeking recognition of a non-enumerated bona fide hedging position would be able to file one application for relief, only to an exchange, rather than to both an exchange with respect to exchange-set limits and to the Commission with respect to federal limits.[997]

Comments Received

Exchange Authority Under the Proposal

The Commission received some comments on its 2016 Supplemental Position Limits Proposal that addressed concerns only marginally responsive to that proposal; the Commission will address those comments in connection with the relevant provisions.[998]

Several commenters supported the Commission's proposal to allow exchanges to recognize non-enumerated bona fide hedge positions with respect to federal speculative position limits;[999] on the other hand, some commenters expressed views against any Commission involvement in the exchange-administered exemption process. That is, according to those commenters, exchanges should be given full discretion or greater leeway to manage an exemption process without Commission interference.[1000] In addition, a commenter requested that the Commission provide additional regulatory certainty for end-users, including that the Commission should simply expand the DCM's current authority to grant bona fide hedge exemptions and maintain the Commission's current oversight role in respect of DCM processes and rules under the DCM Core Principles.[1001]

Similarly, some commenters expressed the view that there could be circumstances where multiple

[993] CEA section 4a(c)(1), 7 U.S.C. 6a(c)(1). *See also* 2016 Position Limits Supplemental Proposal, n. 65.

[994] Rulebooks for some DCMs can be found in the links to their associated documents on the Commission's Web site at *http://sirt.cftc.gov/SIRT/SIRT.aspx?Topic=TradingOrganizations*.

[995] The Commission based this view on its long experience overseeing DCMs and their compliance with the requirements of CEA section 5 and part 38 of the Commission's regulations, 17 CFR part 38. As the Commission noted in the 2016 Supplemental Position Limits Proposal, under part 38, a DCM must comply, on an initial and ongoing basis, with twenty-three Core Principles established in section 5(d) of the CEA, 7 U.S.C. 7(d), and part 38 of the CFTC's regulations and with the implementing regulations under part 38. The Division of Market Oversight's Market Compliance Section conducts regular reviews of each DCM's ongoing compliance with core principles through the self-regulatory programs operated by the exchange in order to enforce its rules, prevent market manipulation and customer and market abuses, and ensure the recording and safe storage of trade information. These reviews are known as rule enforcement reviews (''RERs''). Some periodic RERs examine a DCM's market surveillance program for compliance with Core Principle 4, Monitoring of Trading, and Core Principle 5, Position Limitations or Accountability. On some occasions, these two types of RERs may be combined in a single RER. Market Compliance can also conduct horizontal RERs of the compliance of multiple exchanges in regard to particular core principles. In conducting an RER, the Division of Market Oversight (DMO) staff examines trading and compliance activities at the exchange in question over an extended time period selected by DMO, typically the twelve months immediately preceding the start of the review. Staff conducts extensive review of documents and systems used by the exchange in carrying out its self-regulatory responsibilities; interviews compliance officials and staff of the exchange; and prepares a detailed written report of findings. In nearly all cases, the RER report is made available to the public and posted on CFTC.gov. *See* materials regarding RERs of DCMs at *http://www.cftc.gov/IndustryOversight/TradingOrganizations/DCMs/dcmruleenf* on the Commission's Web site. Recent RERs conducted by DMO covering DCM Core Principle 5 and exemptions from position limits have included the Minneapolis Grain Exchange, Inc. (''MGEX'') (June 5, 2015), ICE Futures U.S. (July 22, 2014), the Chicago Mercantile Exchange (''CME'') and the Chicago Board of Trade (''CBOT'') (July 26, 2013), and the New York Mercantile Exchange (May 19, 2008). While DMO may sometimes identify deficiencies or make recommendations for improvements, it is the Commission's view that it should be permissible for DCMs to process applications for exchange recognition of positions as non-enumerated bona fide hedging positions. Consistent with the fifteen SEF core principles established in section 5h(f) of the CEA, 7 U.S.C. 7b–3(f), and with the implementing regulations under part 37, 17 CFR part 37, the Commission will perform similar RERs for SEFs. The Commission's preliminary view is that it should be permissible for SEFs to process applications as well, after obtaining the requisite experience administering exchange-set position limits discussed below. *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38469, n. 126 and accompanying text.

[996] Since the enactment of the Dodd-Frank Act, Commissioners, CFTC staff, and public officials have expressed repeatedly and publicly that Commission resources have not kept pace with the CFTC's expanded jurisdiction and increased responsibilities. The Commission anticipates there may be hundreds of applications for non-enumerated bona fide hedging positions. This is based on the number of exemptions currently processed by DCMs. For example, under the existing process, during the period from June 15, 2011 to June 15, 2012, the Market Surveillance Department of ICE Futures U.S. received 142 exemption applications, 121 of which related to bona fide hedging position requests, while 21 related to arbitrage or cash-and-carry requests; 92 new exemptions were granted. Rule Enforcement review of ICE Futures U.S., July 22, 2014, p. 40. Also under the existing process, during the period from November 1, 2010 to October 31, 2011, the Market Surveillance Group from the CME Market Regulation Department took action on and approved 420 exemption applications for products traded on CME and CBOT, including 114 new exemptive applications, 295 applications for renewal, 10 applications for increased levels, and one temporary exemption on an inter-commodity spread. Rule Enforcement Review of the Chicago Mercantile Exchange and the Chicago Board of Trade, July 26, 2013, p. 54. These statistics are now a few years old, and it is possible that the number of applications under the processes outlined in this proposal will increase relative to the number of applications described in the RERs. The CFTC would need to shift substantial resources, to the detriment of other oversight activities, to process so many requests and applications and has determined, as described below, to permit exchanges to process applications initially. The Commission anticipates it will regularly, as practicable, check a sample of the exemptions granted, including in cases where the facts warrant special attention, retrospectively as described below, including through RERs.

[997] One commenter specifically requested that the Commission streamline duplicative processes. CL–AGA–60382 at 12 (stating that ''AGA . . . urges the Commission to ensure that hedge exemption requests and any hedge reporting do not require duplicative filings at both the exchanges and the Commission, and therefore recommends revising the rules to streamline the process by providing that an applicant need only apply to and report to the exchanges, while the Commission could receive any necessary data and applications by coordinating data flow between the exchanges and the Commission.''). *See also* CL–Working Group–60396 (explaining that ''To avoid employing duplicative efforts, the Commission should simply rely on DCMs to administer *bona fide* hedge exemptions from federal speculative position limits as they carry out their core duties to ensure orderly markets.'').

[998] One commenter expressed the view that Class III milk should not be subject to the prohibition on holding cross commodity hedge positions in the spot month or during the last five days, because it is a cash settled contract. CL–DFA–60927 at 5. The Commission is addressing Class III milk separately.

[999] CL–NMPF–60956 at 2; CL–ISDA–60931 at 6–7; CL–API–60939 at 4; CL–NFP–60942 at 6–8; and CL–IECAssn–60949 at 3–4.

[1000] CL–CME–60926 at 7; CL–NGFA–60941 at 3.

[1001] CL–NFP–60942 at 6–8.

commercial firms face similar risks and require recognition of positions as non-enumerated bona fide hedges for the same purpose, and there should be a method for a generic recognition of non-enumerated bona fide hedge positions for commercial firms meeting satisfy specified facts and circumstances, allowing an exchange to announce generic recognition of non-enumerated bona fide hedges for hedgers that satisfy certain facts and circumstances; to allow exchange to announce generic recognition for hedgers that certain specified facts.[1002]

Others did not support providing exchanges with such authority. Instead, those commenters asserted that only the Commission can appropriately and comprehensively administer exemptions to federal limits,[1003] or cited concerns with respect to conflicts of interest that could arise between for-profit exchanges and their exemption-seeking customers.[1004] In the alternative, several of these commenters recommended that the Commission make any final non-enumerated bona fide hedging position determinations, or that exchanges have a limited advisory role with respect to granting exemptions. One commenter expressed the view that it is concerned that the Commission's constrained resources will prevent the Commission from effectively overseeing self-regulatory organizations' recognition of bona fide hedging position exemptions. The commenter suggested that the Commission at least provide guidance regarding what is the Commission's authority in the event that an exchange-managed position accountability level fails in numerous contracts to prevent speculation, or raises other concerns.[1005] Further to this point, the commenter expressed the view that it was concerned that granting exemptions from position limits for swaps that are traded by high frequency trading strategies will exacerbate price volatility to the detriment of commercial hedgers by increasing momentum or rumor trading and the costs of hedging in such a price volatile environment. The commenter believes that this will impact the Commission's ability to review and oversee exchange exemptions, especially if the Commission does not have access to open interest swap data and the intra-day high frequency trading data to determine whether such exchange-granted exemption is economically appropriate.[1006]

Implementation Timeline

Regarding implementation of final regulations, one commenter requested that the CFTC provide a sufficient phase-in period for exchanges to review non-enumerated hedges ahead of implementation because it is hard to discern the number of current positions that will not be considered bona fide hedging positions in the proposed rule unless granted a non-enumerated bona fide hedging position e exemption from an exchange.[1007]

Commission Reproposal Regarding § 150.9

As explained further below, in this Reproposal, the Commission is adopting certain amendments to the proposed § 150.9 and providing certain clarifications. In response to various general comments and recommendations for the non-enumerated bona fide hedging position process, the Commission provides the following responses.

Exchange Authority Under Reproposed § 150.9

In response to comments that the Commission should give exchanges greater leeway or discretion for purposes of federal position limits in the exemption process and expand DCM's current authority to grant bona fide hedge exemptions, the Commission believes, as noted above, that it would be an illegal delegation to give full discretion to exchanges to recognize positions or transactions as bona fide hedging positions, for purposes of federal position limits, without reasonably fixed statutory standards (such as the requirement that exchanges use the Commission's bona fide hedging position definition, which incorporates the standards of CEA section 4a(c)), and with no ability for the Commission to make a de novo review.[1008] Instead, as observed above, the Commission believes it has the authority to provide exchanges with the ability to do so pursuant to reasonably fixed statutory standards and subject to CFTC de novo review.[1009]

Similarly, regarding requests to provide exchanges with a method for a generic recognition of a non-enumerated bona fide hedging position that allows an exchange to announce generic recognition of non-enumerated bona fide hedging positions for hedgers that satisfy certain facts and circumstances, the Commission notes that, as discussed above, it would be an illegal delegation of Commission authority to give full discretion to exchanges to recognize positions or transactions as enumerated bona fide hedging positions without reasonably fixed statutory standards, and without review by the Commission, for purposes of federal position limits. Instead, the Commission points out that any exchange can petition the Commission under § 13.2 for recognition of a typical position as an enumerated bona fide hedging position if the exchange believes there is a fact pattern that is so certain as to not require a facts and circumstances review.

In this light, the Commission is reproposing a consistent approach, subject to amendments described below, for processing recognitions of bona fide hedging positions for purposes of federal position limits (*i.e.,* a standard process that the Commission, exchanges and market participants know and understand). As was noted in the 2016 Position Limits Proposal, the Commission believes that the consistent approach under reproposed § 150.9 should increase administrative certainty for applicants seeking recognition of non-enumerated bona fide hedging positions in the form of reduced application-production time by market participants and reduced response time by exchanges and reduce duplicative efforts because applicants would be saved the expense of applying to both an exchange for relief from exchange-set

[1002] CL–EEI–EPSA–60925 at 9 (noting also that ''unlike a hedge exemption, the exchanges are not granting a firm specific quantity of bona fide hedging contracts but, rather, are validating the bona fide nature of a hedge transaction''); CL–COPE–60932 at 8–9 (recommending that ''[t]he Supplemental NOPR should be revised to permit the DCM to generically recognize a non-enumerated bona fide hedge in cases where multiple commercial firms have sought a non-enumerated bona fide hedge for a similar risk, based upon similar circumstances.'').

[1003] CL–Better Markets–60928 at 3–5; CL–Public Citizen–60940 at 3; CL–PMAA–NEFI–60952 at 2; CL–AFR–60953 at 2–3; CL–RER1–60961 at 1.

[1004] CL–Public Citizen–60940 at 3; CL–PMAA–NEFI–60952 at 2; CL–RER2–60962 at 1; CL–AFR–60953 at 2–3; CL–RER1–60961 at 1; CL–PMAA–NEFI–60952 at 2; CL–RER2–60962 at 1; CL–Better Markets–60928 at 3–5; CL–Public Citizen–60940 at 1–2; CL–AFR–60953 at 3–4.

[1005] CL–IATP–60951 at 2.

[1006] CL–IATP–60951 at 6.

[1007] CL–NCFC–60930 at 5.

[1008] *See supra* section G.1. (discussing the Commission's authority to adopt § 150.9); *see also* discussion regarding adoption of § 150.9(d).

[1009] As observed above, the Second Circuit found in *Sunshine Anthracite Coal Co.* v. *Adkins,* that in light of statutory provisions vesting the SEC with power to approve or disapprove NASD's rules according to reasonably fixed statutory standards, and the fact that NASD disciplinary actions are subject to SEC review, there was ''no merit in the contention that the Maloney Act unconstitutionally delegates power to the NASD.'' *R.H. Johnson* v. *Securities and Exchange Commission,* 198 F. 2d 690, 695 (2d Cir. 1952). *See supra* discussion under preamble section G.1; *see also* preamble discussion regarding the adoption of § 150.9(d).

position limits and to the Commission for relief from federal limits.[1010]

The Commission, however, clarifies that exchanges can recognize strategies as non-enumerated bona fide hedging positions for purposes of federal position limits (including those that the Commission has not enumerated) so long as a facts-and-circumstances review leads the exchange to believe that such strategies meet the definition of bona fide hedging position. Further, regarding comments that exchanges should not have authority to grant exemptions, the Commission disagrees and believes the exchange's experience administering position limits to its actively traded contract, and the Commission's de novo review of exchange determinations that positions are bona fide hedging positions (afterwards) are adequate to guard against or remedy any conflicts of interest. The Commission points out that it has had a long history of cooperative enforcement of position limits with DCMs and, in addition notes that when recognizing non-enumerated bona fide hedging positions for purposes of federal limits, exchanges are required to use the Commission's bona fide hedging position definition.[1011]

As to the concerns that allowing bona fide hedging position determinations for swap positions that are traded by high frequency trading strategies will exacerbate price volatility to the detriment of commercial hedgers and impact the Commission's ability to review and oversee exchange determinations (especially if the Commission does not have access to open interest swap data and the intraday high frequency trading data to determine whether such exchange-granted determination is economically appropriate), the Commission notes that it does have access to open interest swap data, trade data and order data. The Commission views its access to open interest swap data, trade data and order data as well as its ability under § 150.9 to review all exchange recognitions as sufficient to allow it to carry out its responsibilities under the Act.

General Reproposal Under § 150.9

Regarding implementation timing, the Commission is proposing to implement a delayed compliance date after publication of a final rule, as discussed above.[1012]

3. Proposed § 150.9(a)—Requirements for a Designated Contract Market or Swap Execution Facility To Recognize Non-Enumerated Bona Fide Hedging Positions

a. Proposed § 150.9(a)(1)

Proposed Rule

The Commission contemplated in proposed § 150.9(a)(1) that exchanges may voluntarily elect to process non-enumerated bona fide hedging position applications by filing new rules or rule amendments with the Commission pursuant to part 40 of the Commission's regulations. The Commission anticipated that, consistent with current practice, most exchanges will self-certify such new rules or rule amendments pursuant to § 40.6. The Commission expected that the self-certification process should be a low burden for exchanges, especially for those that already recognize non-enumerated positions meeting the general definition of bona fide hedging position in § 1.3(z)(1).[1013] The Commission explained its view that allowing DCMs to continue to follow current practice, and extend that practice to exchange recognition of non-enumerated bona fide hedging positions for purposes of the federal position limits, would permit the Commission to more effectively allocate its limited resources to oversight of the exchanges' actions.[1014]

Proposed § 150.9(a)(1) provided that exchange rules must incorporate the general definition of bona fide hedging position in § 150.1. It also provided that, with respect to a commodity derivative position for which an exchange elects to process non-enumerated bona fide hedging position applications, (i) the position must be in a commodity derivative contract that is a referenced contract; (ii) the exchange must list such commodity derivative contract for trading; (iii) such commodity derivative contract must be actively traded on such exchange; (iv) such exchange must have established position limits for such commodity derivative contract; and (v) such exchange must have at least one year of experience administering exchange-set position limits for such commodity derivative contract. The requirement for one year of experience was intended as a proxy for a minimum level of expertise gained in monitoring futures or swaps trading in a particular physical commodity.

The Commission believed that the exchange non-enumerated bona fide hedging position process should be limited only to those exchanges that have at least one year of experience overseeing exchange-set position limits in an actively traded referenced contract in a particular commodity because an individual exchange may not be familiar enough with the specific needs and differing practices of the commercial participants in those markets for which the exchange does not list any actively traded referenced contract in a particular commodity. Thus, if a referenced contract is not actively traded on an exchange that elects to process non-enumerated bona fide hedging position applications for positions in such referenced contract, that exchange might not be incentivized to protect or manage the relevant commodity market, and its interests might not be aligned with the policy objectives of the Commission as expressed in CEA section 4a. The Commission expected that an individual exchange will describe how it will determine whether a particular listed referenced contract is actively traded in its rule submission, based on its familiarity with the specific needs and

[1010] *See, e.g.,* 2016 Position Limits Proposal at 38470, 38488.

[1011] *See* § 150.9(a)(1).

[1012] *See* discussion under Proposed Compliance Date, above; *see also* § 150.2(e)(1).

[1013] DCMs currently process applications for exemptions from exchange-set position limits for non-enumerated bona fide hedging positions and enumerated anticipatory bona fide hedges, as well as for exemptions from exchange-set position limits for spread positions, pursuant to CFMA-era regulatory guidance. *See* 2016 Supplemental Position Limits Proposal, n. 102, and accompanying text. This practice continues because, among other things, the Commission has not finalized the rules proposed in the December 2013 Position Limits Proposal.

As noted above and as explained in the December 2013 Position Limits Proposal, while current § 150.5 regarding exchange-set position limits pre-dates the CFMA ''the CFMA core principles regime concerning position limitations or accountability for exchanges had the effect of undercutting the mandatory rules promulgated by the Commission in § 150.5. Since the CFMA amended the CEA in 2000, the Commission has retained § 150.5, but only as guidance on, and acceptable practice for, compliance with DCM core principle 5.'' December 2013 Position Limits Proposal, 78 FR at 75754.

The DCM application processes for bona fide hedging position exemptions from exchange-set position limits generally reference or incorporate the general definition of bona fide hedging position contained in current § 1.3(z)(1), and the Commission believes the exchange processes for approving non-enumerated bona fide hedging position applications are at least to some degree informed by the Commission process outlined in current § 1.47.

[1014] If the Commission becomes concerned about an exchange's general processing of non-enumerated bona fide hedging position applications, the Commission may review such processes pursuant to a periodic rule enforcement review or a request for information pursuant to § 37.5. Separately, under proposed § 150.9(d), the proposal provides that the Commission may review a DCM's determinations in the case of any specific non-enumerated bona fide hedging position application.

differing practices of the commercial participants in the relevant market.[1015]

The Commission was also mindful that some market participants, such as commercial end users in some circumstances, may not be required to trade on an exchange, but may nevertheless desire to have a particular derivative position recognized as a non-enumerated bona fide hedging position. The Commission noted its belief that commercial end users should be able to avail themselves of an exchange's non-enumerated bona fide hedging position application process in lieu of requesting a staff interpretive letter under § 140.99 or seeking CEA section 4a(a)(7) exemptive relief. This is because the Commission believed that exchanges that list particular referenced contracts would have enough information about the markets in which such contracts trade and would be sufficiently familiar with the specific needs and differing practices of the commercial participants in such markets in order to knowledgeably recognize non-enumerated bona fide hedging positions for derivatives positions in commodity derivative contracts included within a particular referenced contract. The Commission also viewed this to be consistent with the efficient allocation of Commission resources.

Consistent with the restrictions regarding the offset of risks arising from a swap position in CEA section 4a(c)(2)(B), proposed § 150.9(a)(1) would not permit an exchange to recognize a non-enumerated bona fide hedging position involving a commodity index contract and one or more referenced contracts. That is, an exchange may not recognize a non-enumerated bona fide hedging position where a bona fide hedging position could not be recognized for a pass through swap offset of a commodity index contract.[1016]

Comments on Proposed § 150.9(a)(1)

Requirement That Exchanges Recognize Non-Enumerated Bona Fide Hedging Positions Consistent With the General Bona Fide Hedging Definition

In connection with the requirement under § 150.9 to apply the bona fide hedging definition to recognitions, two commenters requested that the Commission specifically allow exchanges to recognize anticipatory merchandising as a non-enumerated bona fide hedging positions should the facts and circumstances warrant including those rejected strategies [transactions or positions that fail to meet the 'change in value' requirement or the 'economically appropriate test'].[1017]

Another commenter expressed the view that the Commission should extend the process proposed in the 2016 Supplemental Position Limits Proposal to include risk management exemptions.[1018] The commenter acknowledged but disagrees with the Commission's view that such risk management exemptions would not be allowed under the statutory standards for a bona fide hedging position, and suggests that the Commission could use CEA section 4a(a)(7) authority to provide exemptions for risk management positions.

A commenter recommended that the rules clarify that the Exchanges may recognize and grant exemptions on the basis of a strategy, or hedging need, or a combination of strategies or hedging requirements associated with managing an ongoing business.[1019]

Separately, one commenter recommended that ''the Commission should confirm that exchanges may continue to adopt their own rules for exemptions from speculative position limits for futures contracts that are subject to DCM limits, but not to federal limits,'' [1020] while two others stated that the Commission should confirm that the 2016 Supplemental Position Limits Proposal's ''prescriptive procedures'' will not apply to exemptions involving exchange-set limits lower than federally-set levels, or where the exchanges set the limits themselves.[1021]

Requests for Recognition of Non-Enumerated Bona Fide Hedging Positions in the Spot Month

A commenter expressed the view that the Commission should not ''categorically prohibit exchanges from granting non-enumerated and anticipatory hedge exemptions, as appropriate, during the spot month'' and reminded the Commission that orderly trading requirements remain applicable to all positions, as provided under the bona fide hedging position definition. The commenter further expressed the view that the statutory definition of *bona fide* hedging position allows for such recognition during the spot month and that a ''one-size-fits-all'' prohibition will ''unnecessarily restrict commercially reasonable hedging activity during the spot month.'' [1022]

Several commenters were generally against the application of the five-day rule to non-enumerated bona fide hedging position exemptions, and recommended that the Commission authorize the exchanges to grant non-enumerated hedge and spread exemptions during the last five days of trading or the spot period, and other alternatives and proposed regulation text.[1023]

Standards Exchanges Must Meet To Provide Recognitions

Several commenters recommended that the Commission not adopt the proposed ''active trading'' and ''one year experience'' requirements regarding a DCM's qualification to administer exemptions from federal position limits.[1024] One commenter requested removal of the ''actively traded'' requirement, expressing concerns that, based on its understanding, the requirement would impose an ''absolute prohibition'' on exchange-administered exemptions for new contracts of at least one year.[1025] Similarly, a commenter stated that the standard ''would arbitrarily limit competition and operate

[1015] For example, a DCM (''DCM A'') may list a commodity derivative contract (''KX,'' where ''K'' refers to contract and ''X'' refers to the commodity) that is a referenced contract, actively traded, and DCM A has the requisite experience and expertise in administering position limits in that one contract KX. DCM A can therefore recognize non-enumerated bona fide hedging positions in contract KX. But DCM A is not limited to recognition of just that one contract KX–DCM A can also recognize any other contract that falls within the meaning of referenced contract for commodity X. So a market participant could, for example, apply to DCM A for recognition of a position in any contract that falls within the meaning of referenced contract for commodity X. However, that market participant would still need to seek separate recognition from each exchange where it seeks an exemption from that other exchange's limit for a commodity derivative contract in the same commodity X.

[1016] This is consistent with the Commission's interpretation in the December 2013 Position Limits Proposal that CEA section 4a(c)(2)(b) is a direction from Congress to narrow the scope of what constitutes a bona fide hedge in the context of index trading activities. ''Financial products are not substitutes for positions taken or to be taken in a physical marketing channel. Thus, the offset of financial risks from financial products is inconsistent with the proposed definition of bona fide hedging for physical commodities.'' December 2013 Position Limits Proposal, 78 FR at 75740. *See also* the discussion of the temporary substitute test in the December 2013 Position Limits Proposal, 78 FR at 75708–9.

[1017] CL–ICE–60929 at 12; CL–Working Group–60947 at 6.

[1018] CL–AMG–60946 at 6–7.

[1019] CL–CCI–60935 at 5.

[1020] CL–FIA–60937 at 4.

[1021] CL–ICE–60929 at 7; CL–Working Group–60947 at 14.

[1022] CL–ICE–60929 at 9.

[1023] CL–ICE–60929 at 22; CL–NCGA–NGSA–60919 at 13; CL–CME–60926 at 6 and 8; CL–API–60939 at 3; CL–FIA–60937 at 3 and 12; CL–Working Group–60947 at 7–9; CL–NCC–ACSA–60972 at 2; CL–CMC–60950 at 9–11; CL–ISDA–60931 at 3 and 10; CL–CCI–60935 at 8–9; CL–MGEX–60936 at 11; CL–FIA–60937 at 10, 11; CL–MGEX–60936 at 11.

[1024] CL–CCI–60935 at 3–4; CL–CME–60926 at 13; CL–FIA–60937 at 9; CL–CMC–60950 at 3; CL–Working Group–60947 at 10; CL–IECAssn–60949 at 12–13.

[1025] CL–CMC–60950 at 3.

as a bar to the establishment of new exchanges and new contracts.'' [1026]

In the alternative, one commenter argues that one year of experience in administering position limits in similar contracts within a particular ''asset class'' would be a more reasonable requirement.[1027] In addition, a commenter expressed the view that the Commission should not define ''actively traded'' in terms of minimum monthly volume.[1028]

Previously Granted Hedge Exemptions

One commenter expressed the view that since the exchanges have been working with commercial end user for several decades and currently have a process under § 1.3(z) that may contain specific scenarios that work well and are not listed in the 2016 Position Limits Proposal, the Commission should deem every currently recognized hedge strategy by any exchange as a non-enumerated bona fide hedging position which would eliminate disruption and encourage the autonomy of the exchanges.[1029]

The commenter also expressed the view that, with respect to the status of previously exchange-recognized non-enumerated bona fide hedging positions for which such exchange no longer provides an annual review, the non-enumerated bona fide hedging positions should remain a non-enumerated bona fide hedging position and the participants utilizing that strategy should have ample notice that the exchange will no longer provide the annual review in order to allow time for the individual entity to apply to the CFTC directly for a non-enumerated bona fide hedging position exemption.[1030]

Recognition of OTC Positions as Bona Fide Hedges

Another commenter requested Commission clarification regarding an exchange's obligation with respect to recognizing and monitoring non-enumerated bona fide hedging position determinations for OTC positions. The commenter cited to preamble language to support the possibility of an obligation, but argued that the text of proposed § 150.9 does not mention or contemplate such requests for OTC positions. The commenter also questioned whether such recognition is feasible given the exchanges' lack of visibility into OTC markets.[1031]

Commission Reproposal Regarding § 150.9(a)(1) [1032]

The Commission is reproposing the rule, as originally proposed, subject to the amendments described below.

Requirement That Exchanges Recognize Non-Enumerated Bona Fide Hedging Positions Consistent With the General Bona Fide Hedging Position Definition

Regarding comments that the Commission should permit the recognition of anticipatory merchandising as non-enumerated bona fide hedging strategies, as noted above, while exchanges' recognition of non-enumerated bona fide hedging positions must be consistent with the Commission's bona fide hedging position definition, the Commission agrees that exchanges should, in each case, make a facts-and-circumstances determination as to whether to recognize an anticipatory hedge as a non-enumerated bona fide hedging position, consistent with the Commission's recognition ''that there can be a gradation of probabilities that an anticipated transaction will occur.'' [1033]

In response to the request that the Commission expand the proposed bona fide hedging position recognition process to include risk management exemptions, the Commission notes that this suggestion is contrary to the intent of Congress (to narrow the bona fide hedging position definition to preclude commodity index hedging, a.k.a. risk management exemptions).

Regarding comments requesting clarification on exchange authority to recognize as bona fide hedging positions multiple hedging strategies, the Commission clarifies that a single application to an exchange can specify and apply to multiple hedging strategies or needs.

As to comments requesting clarification regarding whether the proposed application process applies to exchange-set limits, the Commission notes that the requirements of reproposed § 150.9(a) addresses processes for recognition of bona fide hedge positions for purposes of federal limits and not exemption processes such as those exchanges currently implement and oversee for any exchange-set limits. In addition, such processes for exchange-set limits that are lower than the federal limit could differ as long as the exemption provided by the exchange is capped at the level of the applicable federal limit in § 150.2.[1034]

Requests for Recognition of Non-Enumerated Bona Fide Hedging Positions in the Spot Month

The Commission considered the recommendations that the Commission: Allow exchanges to recognize a position as a bona fide hedging position for up to a five-day retroactive period in circumstances where market participants need to exceed limits to address a sudden and unforeseen hedging need; specifically authorize exchanges to recognize positions as bona fide hedging positions and grant spread exemptions during the last five days of trading or less, and/or delegate to the exchanges for their consideration the decision whether to apply the five-day rule to a particular contract after their evaluation of the particular facts and circumstances. As the Commission clarified above, the reproposed rules do not apply the prudential condition of the five-day rule to non-enumerated hedging positions other than to pass through swap offsets.[1035] Therefore, as reproposed, the five-day rule would only apply to certain positions (pass-through swap offsets, anticipatory and cross-commodity hedges).[1036] However, to provide exchanges with flexibility, in regards to exchange process under § 150.9, the Commission will allow exchanges to waive the five-day rule on a case-by-case basis.[1037] As the Commission noted above, it expects that exchanges will carefully consider whether allowing retroactive recognition of a positions as a non-enumerated bona fide hedge would, as raised by one commenter, diminish the overall integrity of the process. In

[1026] CL–IECAssn–60949 at 12–13.

[1027] CL–CME–60926 at 14.

[1028] CL–IECAssn–60949 at 13.

[1029] CL–IECAssn–60949 at 11–12.

[1030] *Id.* at 12.

[1031] CL–CME–60926 at 11–12.

[1032] *See* the 2016 Supplemental Position Limits Proposal, 81 FR at 38469–71 (providing further explanation of proposed § 150.9(a)(1)).

[1033] December 2013 Position Limits Proposal, 78 FR at 75719.

[1034] Similarly, as noted above, reproposed § 150.5(a)(2)(i) provides that any exchange may grant exemptions from any speculative position limits it sets under paragraph § 150.5(a)(1), provided that such exemptions conform to the requirements specified in § 150.3, and provided further that any exemptions to exchange-set limits not conforming to § 150.3 are capped at the level of the applicable federal limit in § 150.2.

[1035] *See* the discussion regarding the five-day rule in connection with the definition of bona fide hedging position and in the discussion of 150.9 (Process for recognition of positions as non-enumerated bona fide hedging positions).

[1036] *See* § 150.1 definition of bona fide hedging position sections (2)(ii)(A), (3)(iii), (4), and (5) (Other enumerated hedging position). To provide greater clarity as to which bona fide hedging positions the five-day rule applies, the reproposed rules reorganize the definition.

[1037] In addition, reproposed § 150.5(a)(2)(ii) (Application for exemption) permits exchanges to adopt rules that allow a trader to file an application for an enumerated bona fide hedging exemption within five business days after the trader assumed the position that exceeded a position limit, and adopted a similar modification to 150.5(b)(5)(i).

addition, the Commission also points out that exchanges should carefully consider whether to adopt in those rules the two safeguards noted by commenters: (i) Requiring market participants making use of the retroactive application to demonstrate that the applied-for hedge was required to address a sudden and unforeseen hedging need; and (ii) providing that if the emergency hedge recognition was not granted, exchange rules would continue to require the applicant to unwind its position in an orderly manner and also would deem the applicant to have been in violation for any period in which its position exceeded the applicable limits.

Standards Exchanges Must Meet To Provide Recognitions

Regarding comments on the ''active trading'' and ''one year of experience'' requirements under proposed § 150.9(a)(1)(v), as noted in the 2016 Supplemental Position Limits Proposal preamble [1038] and above, the Commission is not persuaded that an exchange with no active trading and no experience would have their interests aligned with the Commission's policy objectives in CEA section 4a. However, it is clear from the comments that some interpreted the requirement as a narrower standard than intended.

The Commission is, therefore, amending § 150.9(a)(1)(v) to clarify that the active one-year of experience requirement can be met by any contract listed in the particular referenced contract.[1039] As such, the Commission is reproposing § 150.9(a)(1)(v) to provide that the exchange has at least one year of experience and expertise administering position limits for ''a particular commodity'' rather than for ''such commodity derivative contract.'' Further, in response to concerns that the standard would limit competition and operate as a bar to the establishment of new exchanges and new contracts, the Commission notes that experience manifests in the people carrying out surveillance in a commodity rather than in an institutional structure. An exchange's experience could be demonstrated through the relevant experience of the surveillance staff regarding the particular commodity. In fact, the Commission has historically reviewed the experience and qualifications of exchange regulatory divisions when considering whether to designate a new exchange as a contract market or to recognize a facility as a SEF; as such exchanges are new, staff experience has clearly been gained at other exchanges.[1040]

In addition, regarding the Commission's authority to adopt this standard, the Commission notes that CEA section 4a(c) provides that the Commission ''shall'' define what constitutes a bona fide hedging transaction or position. In light of this responsibility, the Commission believes it is important that exchanges authorized to recognize non-enumerated bona fide hedging positions have experience (as indicated by their one year of experience regulating a particular contract) and interests (as indicated by their actively traded contract) that are aligned with the Commission's interests. The commenter provides no alternatives to the one-year experience in the actively traded contract as proxies for an exchange's interests being aligned with that of the Commission.

The Commission clarifies, however, that an exchange can petition the Commission, pursuant to § 140.99, for a waiver of the one-year experience requirement if such exchange believes that their experience and interests are aligned with the Commission's interests with respect to recognizing non-enumerated bona fide hedging positions.

Previously Granted Hedge Exemptions

With respect to comments regarding currently recognized exchange-granted non-enumerated bona fide hedging position exemptions, as noted above, the Commission believes the statutory directive to define bona fide hedging position narrows the current § 1.3(z)(1) definition. As a result, currently recognized bona fide hedging strategies may not meet the new narrower bona fide hedging position standards. While certain strategies may not meet the definition of bona fide hedging position reproposed in this rulemaking, to reduce the potential for market disruption by forced liquidations, the Commission proposes, as discussed above, to clarify and expand the relief in § 150.3(f) (previously granted exemptions) to grandfather previously granted risk-management strategies applicable to previously established derivative positions in commodity index contract.[1041]

Regarding comments that exchanges should be required to provide additional notice or phase-out time for any bona fide hedging position recognitions that may expire, the Commission notes that, under reproposed § 150.5, exchanges may issue recognition determinations for one year only. As such a market participant is provided a one-year notice for the potential expiration of the recognition of their position as a non-enumerated bona fide hedging position, and may seek recognition of the position from another (or the same) DCM, or from the CFTC directly prior to the expiration of the one-year period. The Commission is not proposing to authorize exchanges to provide an unlimited recognition of positions as non-enumerated bona fide hedging positions, and is not proposing to require exchanges to provide further notice to market participants prior to the expiration of previous determinations.

Recognition of OTC Positions as Bona Fide Hedging Positions

Regarding comments requesting a clarification with respect to OTC positions, the Commission clarifies that exchanges do not have an obligation to monitor for compliance with OTC-only positions.

[1038] 2016 Supplemental Position Limits Proposal, 81 FR at 38471.

[1039] Regarding the comment that the Commission should not define ''actively traded,'' the Commission concurs, and notes that, as proposed in the 2016 Supplemental Position Limits Proposal, this interpretation will be left to the exchanges' reasonable discretion.

[1040] For example, the Commission reviews the experience of chief compliance officers when reviewing SEF applications. *See* § 37.1501(b)(2) (''Qualifications of chief compliance officer. The individual designated to serve as chief compliance officer shall have the background and skills appropriate for fulfilling the responsibilities of the position.'').

[1041] As stated above, § 150.3(f) provides (1) recognition of the offset of the risk of a pre-existing financial instrument as bona fide using a derivative position, including a deferred derivative contract month entered after the effective date of a final rule, provided a nearby derivative contract month is liquidated (such recognition will not extend such relief to an increase in positions after the effective date of a limit); (2) possible application of previously granted exemptions to pre-existing financial instruments that are within the scope of existing § 1.47 exemptions, rather than only to pre-existing swaps; and (3) recognition of exchange-granted non-enumerated exemptions in non-legacy commodity derivatives outside of the spot month (consistent with the Commission's recognition of risk management exemptions outside of the spot month), provided such exemptions are granted prior to the compliance date of a final rule, and apply only to pre-existing financial instruments as of the effective date of a final rule. These last two were proposed to reduce the potential for market disruption, since a market intermediary would continue to be able to offset risks of pre-effective-date financial instruments, pursuant to previously-granted federal or exchange risk management exemptions. *See supra* discussion of the Commission's reproposed definition for bona fide hedging position; *see also* the discussion regarding the reproposed § 150.3(f). In response to the comment requesting that the Commission use its authority under CEA section 4a(a)(7) to provide exemptions for risk management positions, as noted above, that appears contrary to Congressional intent to narrow the definition of a bona fide hedging position.

b. Proposed § 150.9(a)(2); § 150.9(a)(3); and § 150.9(a)(4)—Application Process

*Proposed Rules.* As proposed, § 150.9(a)(2) would permit an exchange to establish a less expansive application process for non-enumerated bona fide hedging positions previously recognized and published on such exchange's Web site than for non-enumerated bona fide hedging positions based on novel facts and circumstances. This is because the Commission believed that some lesser degree of scrutiny may be adequate for applications involving recurring fact patterns, so long as the applicants are similarly situated. However, the Commission understood that DCMs currently use a single-track application process to recognize non-enumerated positions, for purposes of exchange limits, as within the meaning of the general bona fide hedging position definition in § 1.3(z)(1).[1042] The Commission did not know whether any exchange would elect to establish a separate application process for non-enumerated bona fide hedging positions based on novel versus non-novel facts and circumstances, or what the salient differences between the two processes might be, or whether a dual-track application process might be more likely to produce inaccurate results, *e.g.,* inappropriate recognition of positions that are not bona fide hedging positions within the parameters set forth by Congress in CEA section 4a(c).[1043] In proposing to permit separate application processes for novel and non-novel non-enumerated bona fide hedging positions, the Commission sought to provide flexibility for exchanges, but will insist on fair and open access for market participants to seek recognition of compliant positions as non-enumerated bona fide hedging positions.

The Commission believed that there is a core set of information and materials necessary to enable an exchange to determine, and the Commission to verify, whether the facts and circumstances attendant to a position satisfy the requirements of CEA section 4a(c). Accordingly, the Commission proposed to require in § 150.9(a)(3)(i), (iii) and (iv) that all applicants submit certain factual statements and representations. Proposed § 150.9(a)(3)(i) required a description of the position in the commodity derivative contract for which the application is submitted and the offsetting cash positions.[1044] Proposed § 150.9(a)(3)(iii) required a statement concerning the maximum size of all gross positions in derivative contracts to be acquired during the year after the application is submitted.[1045] Proposed § 150.9(a)(3)(iv) required detailed information regarding the applicant's activity in the cash markets for the commodity underlying the position for which the application is submitted during the past three years.[1046] These proposed application requirements are similar to existing requirements for recognition under current § 1.48 of a non-enumerated bona fide hedge.

The Commission also proposed to require in § 150.9(a)(3)(ii) and (v) that all applicants submit detailed information to demonstrate why the position satisfies the requirements of CEA section 4a(c) [1047] and any other information necessary to enable the exchange to determine, and the Commission to verify, whether it is appropriate to recognize such a position as a non-enumerated bona fide hedge.[1048] The Commission anticipated that such detailed information may include both a factual and legal analysis indicating why recognition is justified for such applicant's position. The Commission expected that if the materials submitted in response to proposed § 150.9(a)(3)(ii) are relatively comprehensive, requests for additional information pursuant to proposed § 150.9(a)(3)(v) would be relatively infrequent. Nevertheless, the Commission believed that it is important to include the requirement in proposed § 150.9(a)(3)(v) that applicants submit any other information necessary to enable the exchange to determine, and the Commission to verify, that it is appropriate to recognize a position as a non-enumerated bona fide hedging position so that DCMs can protect and manage their markets.

Under the proposal, the Commission would permit an exchange to recognize a smaller than requested position for purposes of exchange-set limits. For instance, an exchange might recognize a smaller than requested position that otherwise satisfies the requirements of CEA section 4a(c) if the exchange determines that recognizing a larger position would be disruptive to the exchange's markets. This is consistent with current exchange practice. This is also consistent with DCM and SEF core principles. DCM core principle 5(A) provides that, ''[t]o reduce the potential threat of market manipulation or congestion (especially during trading during the delivery month), the board of trade shall adopt for each contract of the board of trade, as is necessary and appropriate, position limitations or position accountability for speculators.'' [1049] SEF core principle 6(A) contains a similar provision.[1050]

By requiring in proposed § 150.9(a)(3) that all applicants submit a core set of information and materials, the Commission anticipated that all exchanges would develop similar non-

[1042] 17 CFR 1.3(z)(1).

[1043] 7 U.S.C. 6a(c). The Commission noted that it could, under the proposal, review determinations made by a particular exchange, for example, that recognizes an unusually large number of bona fide hedging positions, relative to those of other exchanges.

[1044] *See* § 1.47(b)(1), 17 CFR 1.47(b)(1), requiring a description of the futures positions and the offsetting cash positions.

[1045] *See* § 1.47(b)(4), 17 CFR 1.47(b)(4), requiring the maximum size of gross futures positions which will be acquired during the following year.

[1046] *See* §§ 1.47(b)(6), 1.48(b)(1)(i) and (2)(i), 17 CFR 1.47(b)(6), 1.48(b)(1)(i) and 2(i), requiring three years of history of production or usage.

[1047] Although many commenters have requested that the Commission retain the pre-Dodd Frank Act standard contained in current § 1.3(z), 17 CFR 1.3(z), there is explicit and implicit support in the comments on the December 2013 Position Limits Proposal for pegging what applicants must demonstrate to the current statutory provision as amended by the Dodd-Frank Act. One commenter requested that the Commission ''publicly clarify that hedge positions are bona fide when they satisfy the hedge definition codified by Congress in section 4a(c)(2) of the Act, as added by the Dodd-Frank Act.'' CL–CME–59718 at 46. Another commenter supported a ''process for Commission approval of a 'non-enumerated' hedge that . . . complies with the statutory definition of the term 'bona fide hedge.' '' CL–NGSA–59673 at 2. CEA section 4a(c)(2) contains standards for positions that constitute bona fide hedging positions. The Commission expects that exchanges would consider the Commission's relevant regulations and interpretations, when determining whether a position satisfies the requirements of CEA section 4a(c)(2). However, exchanges may confront novel facts and circumstances with respect to a particular applicant's position, dissimilar to facts and circumstances previously considered by the Commission. In these cases, an exchange may request assistance from the Commission; *see* the discussion of proposed § 150.9(a)(8) in the 2016 Position Limits Supplemental Proposal.

[1048] *See* § 1.47(b)(2), 17 CFR 1.47(b)(2), requiring detailed information to demonstrate that the futures positions are economically appropriate to the reduction of risk in the conduct and management of a commercial enterprise. *See also* § 1.47(b)(3), 17 CFR 1.47(b)(3), requiring, upon request, such other information necessary to enable the Commission to determine whether a particular futures position meets the requirements of the general definition of bona fide hedging. Under current application processes, market participants provide similar information to DCMs, make various representations required by DCMs and agree to certain terms imposed by DCMs with respect to exemptions granted. The Commission has recognized that DCMs already consider any information they deem relevant to requests for exemptions from position limits. *See, e.g.,* Rule Enforcement Review of ICE Futures U.S., July 22, 2014, p. 41.

[1049] CEA section 5(d)(5)(A), 7 U.S.C. 7(d)(5)(A); § 38.300, 17 CFR 38.300. The Commission proposed, consistent with previous Commission determinations, a preliminary finding that speculative position limits are necessary in the December 2013 Position Limits Proposal. December 2013 Position Limits Proposal, 78 FR at 75685.

[1050] CEA Section 5h(f)(6)(A), 7 U.S.C. 7b–3(f)(6)(A); § 38.300, 17 CFR 38.300.

enumerated bona fide hedging position application processes. However, the Commission intended that exchanges have sufficient discretion to accommodate the needs of their market participants. The Commission also intended to promote fair and open access for market participants to obtain recognition of compliant derivative positions as non-enumerated bona fide hedges.

Proposed § 150.9(a)(4) set forth certain timing requirements that an exchange must include in its rules for the non-enumerated bona fide hedge application process. A person intending to rely on an exchange's recognition of a position as a non-enumerated bona fide hedging position would be required to submit an application in advance and to reapply at least on an annual basis. This is consistent with commenters' views and DCMs' current annual exemption review process.[1051] Proposed § 150.9(a)(4) would require an exchange to notify an applicant in a timely manner whether the position was recognized as a non-enumerated bona fide hedging position or rejected, including the reasons for any rejection.[1052] On the other hand, and consistent with the status quo, proposed § 150.9(a)(4) would allow the exchange to revoke, at any time, any recognition previously issued pursuant to proposed § 150.9 if the exchange determined the recognition is no longer in accord with section 4a(c) of the Act.[1053]

The Commission did not propose to prescribe time-limited periods (*e.g.,* a specific number of days) for submission or review of non-enumerated bona fide hedge applications. The Commission proposed only to require that an applicant must have received recognition for a non-enumerated bona fide hedging position before such applicant exceeds any limit then in effect, and that the exchange administer the process, and the various steps in the process, in a timely manner. This means that an exchange must, in a timely manner, notify an applicant if a submission is incomplete, determine whether a position is a non-enumerated bona fide hedging position, and notify an applicant whether a position will be recognized, or the application rejected. The Commission anticipated that rules of an exchange may nevertheless set deadlines for various parts of the application process. The Commission does not believe that reasonable deadlines or minimum review periods are inconsistent with the general principle of timely administration of the application process. An exchange could also establish different deadlines for a dual-track application process. The Commission believed that the individual exchanges themselves are in the best position to evaluate how quickly each can administer the application process, in order best to accommodate the needs of market participants. In addition to review of an exchange's timeline when it submits its rules for its application process under part 40, the Commission would review the exchange's timeliness in the context of a rule enforcement review.

Comments Received

One commenter expressed the view that it does not support different application processes for novel and non-novel hedges.[1054]

Two commenters expressed the view that the 2016 Supplemental Position Limits Proposal should be revised to eliminate, to the maximum extent possible, the ''overly prescriptive rules'' governing what exchanges must collect from non-enumerated bona fide hedging position applicants and instead give the exchanges more discretion and flexibility to fashion non-enumerated bona fide hedging position rules that are more closely aligned with current hedge approval processes.[1055] Conversely, another commenter recommended that the Commission require a standardized and harmonized process across all participating exchanges for non-enumerated bona fide hedging position applications.[1056]

One commenter recommended that the Commission, to the greatest extent possible, allow the exchanges to administer exemptions for non-enumerated bona fide hedging positions, enumerated bona fide hedging positions, and spread positions in the same manner as they have been to date.[1057]

Several commenters recommended that the Commission not require exchanges to demand and collect three years of cash market information in order to process an entity's application for a non-enumerated bona fide hedging exemption. According to the commenters, it would be burdensome on both the applicant and the exchange, as well as unnecessary and not authorized by the CEA.[1058] As an alternative, commenters cited practices currently authorized for, and practiced by, the exchanges, and that typically only require applicants to provide such data from the preceding year, though the market participant requesting the hedge exemption must stand ready to provide further supporting documentation for the requested exemption on request.[1059]

One commenter expressed the view that exchanges do not need the ''detailed information'' that the 2016 Supplemental Position Limits Proposal requires of market participants seeking an exchange-administered hedge exemption. The commenter believes that requiring an exemption applicant to perform its own legal and economic analysis would be cost prohibitive and impractical. Further, the commenter asserted that it is unclear whether an exchange could still grant an exemption even if it disagrees with an applicant's analysis.[1060]

Some commenters requested clarification regarding the proposed § 150.9(a)(3) requirement with respect to

[1051] *See, e.g.,* statement of Ron Oppenheimer on behalf of the Working Group (supporting an annual non-enumerated bona fide hedge application), statement of Erik Haas, Director, Market Regulation, ICE Futures U.S. (describing the DCM's annual exemption review process), and statement of Tom LaSala, Chief Regulatory Officer, CME Group (envisioning market participants applying for non-enumerated bona fide hedge on a yearly basis), transcript of the EEMAC open meeting, July 29, 2015, at 40, 53, and 58, available at *http://www.cftc.gov/idc/groups/public/@aboutcftc/documents/file/emactranscript072915.pdf.*

[1052] *See, e.g.,* statement of Ron Oppenheimer on behalf of the Working Group (noting that exchanges retain the ability to revoke an exemption if market circumstances warrant), transcript of the EEMAC open meeting, July 29, 2015, at 57, available at *http://www.cftc.gov/idc/groups/public/@aboutcftc/documents/file/emactranscript072915.pdf.*

[1053] As noted above, the 2016 Supplemental Position Limits Proposal did not impair the ability of any market participant to request an interpretation under § 140.99 for recognition of a position as a bona fide hedging position if an exchange rejects their recognition application or revokes recognition previously issued. *See* 2016 Position Limits Supplemental Proposal, n. 78 and accompanying text.

[1054] CL–IECAssn–60949 at 14.

[1055] CL–ETP–60915 at 1; CL–MGEX–60936 at 5–6.

[1056] CL–EDF–60944 at 1–3.

[1057] CL–NCGA–NGSA–60919 at 9.

[1058] CL–NCGA–NGSA–60919 at 10; CL–EEI–EPSA–60925 at 4; CL–ICE–60929 at 8; 16, CL–COPE–60932 at 9; CL–CCI–60935 at 7; CL–COPE–60932 at 9; CL–FIA–60937 at 3; 12, CL–AGA–60943 at 6; CL–AMG–60946 at 3–4; CL–Working Group–60947 at 11; CL–NCGA–NGSA–60919 at 10; CL–CCI–60935 at 7; CL–CME–60926 at 9; CL–FIA–60937 at 3, 12; CL–Working Group–60947 at 11 (footnotes omitted); and CL–ICE–60929 at 8, 16 (noting that in many cases exchanges already have access to this data, or can easily obtain it).

[1059] CL–NCGA–NGSA–60919 at 10; CL–CCI–60935 at 7; CL–CME–60926 at 9; CL–Working Group–60947 at 11 (footnotes omitted); CL–FIA–60937 at 3, 12; CL–Working Group–60947 at 11; CL–NCGA–NGSA–60919 at 10; CL–CCI–60935 at 7; CL–CME–60926 at 9; CL–AGA–60943 at 6; and CL–AMG–60946 at 3–4 (recommending that exchanges have authority to, but not be required to, collect up to 3 years of data).

[1060] CL–CME–60926 at 9. *See also* CL–AMG–60946 at 4 (requesting a clarification that that this demonstration (of how the position meets the definition of a bona fide hedging position does not require submission of legal opinion from counsel which would be ''unduly burdensome'' for market participants).

the compilation of gross positions for every commodity derivative contact that the applicant holds, and whether the proposed regulations are intended to apply to an applicant's maximum size of all gross positions for each and every commodity derivative contract the applicant holds (as opposed to the maximum gross positions in the commodity derivative contract(s) for which the exemption is sought).[1061] In addition, one commenter suggested that ''the Commission should clarify that an application for a non-enumerated hedge or spread exemption only must include derivative positions related to the requested exemption.'' [1062]

One commenter expressed the view that it is concerned regarding how exchanges should coordinate the granting of exemptions with respect to contracts on the same underlying commodities that trade on different exchanges, and requests guidance from the Commission on that matter.[1063]

In connection with proposed § 150.9(a)(4), several commenters expressed the view that the Commission should allow exchanges to recognize an enumerated or non-enumerated bona fide hedging position exemption retroactively in circumstances where market participants need to exceed limits to address a sudden and unforeseen hedging need.[1064]

Commission Reproposal

The Commission has determined to repropose the rule, largely as originally proposed, except that the Commission has revised the regulatory text to: (i) Clarify what the statement must address under § 150.9(a)(3)(iii) and 150.9(a)(3)(iv); and (ii) require only one year of history rather than three years in § 150.9(a)(3)(iv), each as described further below.

Regarding comments that the Commission should not have different application processes for novel vs. non-novel products, (pursuant to proposed § 150.9(a)(2)) the Commission is clarifying that exchanges are authorized but not required to have a different application process for novel and non-novel hedge applications. Further, § 150.9 does not prevent industry from working together to adopt a universal application for novel and non-novel hedges.

Regarding comments on current exchange processes for administering exemptions, and comments regarding the information required in the application process, reproposed § 150.9 would require that exchanges collect a minimum amount of information, and exchanges would have discretion to require additional information. That is, § 150.9 provides parameters for a basic application and processing process for the recognition of non-enumerated bona fide hedging positions; the parameters allow exchanges flexibility, while also facilitating Commission review. Also, the Commission reiterates that reproposed § 150.9 addresses federal limits and not exchange exemption processes, such as those exchanges currently implement and oversee for any exchange-set limits. Such processes for exchange-set limits that are lower than the federal limit could differ as long as the exemption provided by the exchange is capped at the level of the applicable federal limit in § 150.2.

Regarding concerns that § 150.9(a)(3)(ii), as proposed, required an application to include a legal opinion or analysis for exchange recognition of a position as a non-enumerated bona fide hedging position, the Commission clarifies that the regulation does not require applicants to obtain a legal opinion or analysis. Rather, under § 150.9(a)(3), it is the exchange's duty to make a determination regarding whether a contract meets the application requirements; it may ask for additional information than the minimum required if it determines that further information is necessary to make its determination. To further clarify this point, the Commission is proposing the following change to § 150.9(a)(3)(ii) to provide that the exchange require at a minimum ''information to demonstrate why the position satisfies the requirements of section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1,'' rather than ''detailed information.'' The same change is also being proposed for § 150.9(a)(3(iv) for the same reasons.

Regarding interpreting § 150.9(a)(3)(iii) as requiring the inclusion in a non-enumerated bona fide hedging position application of a statement regarding the maximum gross positions to be acquired by the applicant during the year after the application is submitted, the Commission clarifies that the provision requires only information related to the contract for which the application is submitted; consequently, the Commission is reproposing § 150.9(a)(3)(iii) to require a ''statement concerning the maximum size of all gross positions in derivative contracts for which the application is submitted.'' The Commission further clarifies that the statement should be based on a good faith estimate.

In addition, the Commission notes that the minimum information to be required by the exchange under § 150.9(a)(3)(iii), would be for the gross position for the following year, since the applicant will need to reapply each year for exchange recognition of its position as a bona fide hedging position.

With respect to the condition that exchanges require applicants to provide three years of data supporting their application, the Commission is reproposing § 150.9(a)(3)(iv) to require only one year of data.

Regarding commenter concerns about whether or how exchanges should coordinate in granting exemptions consistently across exchanges, the reproposed rules would allow each exchange to use their own expertise to decide which positions should be recognized as bona fide hedging positions and what limit levels to impose for their venue. The Commission notes that it serves in an oversight role to monitor exchange determinations and position limits across exchanges. The Reproposal does not require exchanges to coordinate with respect to making such determinations; however, neither does reproposed § 150.9 prohibit coordination.

Regarding application of the five-day rule to non-enumerated bona fide hedging positions, as the Commission discussed above, the Reproposal does not apply the prudential condition of the five-day rule to non-enumerated bona fide hedging positions. As discussed in connection with the definition of bona fide hedging position and in the context of § 150.5(a),[1065] the five-day rule would only apply to certain positions (pass-through swap offsets, anticipatory and cross-commodity hedges).[1066] However, in regards to exchange processes under § 150.9 (and § 150.10, and § 150.11), the Commission is allowing exchanges to waive the five-day rule on a case-by-case basis.

Regarding exchanges' authority to retroactively recognize positions as bona

[1061] CL–CCI–60935 at 6–7; and (CL–Working Group–60947 at 10).

[1062] CL–FIA–60937 at 4, 13.

[1063] CL–ISDA–60931 at 6–7.

[1064] *See, e.g.,* CL–NCGA–NGSA–60919 at 10–11; CL–EEI–EPSA–60925 at 4; CL–ICE–60929 at 11; CL–ISDA–60931 at 13; CL–FIA–60937 at 13; CL–Working Group–60947 at 13–14; and CL–CME–60926 at 12.

[1065] *See* 2016 Position Limits Supplemental Proposal for the discussion regarding the five-day rule in connection with the definition of bona fide hedging position and in the discussion of § 150.5 (Exchange-set speculative position limits).

[1066] *See* § 150.1 definition of bona fide hedging position sections (2)(ii)(A), (3)(iii), (4), and (5) (Other enumerated hedging position). As noted above, to provide greater clarity as to which bona fide hedge positions the five-day rule applies, the reproposed rules reorganize the definition.

fide hedging positions, reproposed § 150.9(a)(5) would require an applicant to receive exchange recognition in advance of the date that a position would otherwise be in excess of a position limit. Thus, the Reproposal would not permit retroactive recognition of a non-enumerated bona fide hedging position. The Commission preliminarily does not believe that it should authorize an exchange to recognize a non-enumerated bona fide hedging position retroactively, as this may diminish the ability of the Commission to review timely such an exchange determination, potentially diminishing the utility of position limits in preventing unwarranted price fluctuations.[1067] By way of contrast with regard to enumerated bona fide hedging positions, the Commission expects that exchanges will carefully consider whether allowing retroactive recognition of an enumerated bona fide hedging exemption, under reproposed § 150.5, would, as noted by one commenter, diminish the overall integrity of the process. And the exchanges should also consider whether to adopt in those rules the two safeguards noted: (i) Requiring market participants making use of the retroactive application to demonstrate that the applied-for hedge was required to address a sudden and unforeseen hedging need; and (ii) providing that if the emergency hedge recognition was not granted, exchange rules would continue to require the applicant to unwind its position in an orderly manner and also would deem the applicant to have been in violation for any period in which its position exceeded the applicable limits.[1068]

c. Proposed 150.9(a)(5) and Commission Reproposal

Proposed § 150.9(a)(5) made it clear that the position will be deemed to be recognized as a non-enumerated bona fide hedging position when an exchange recognizes it; proposed § 150.9(d) provided the process through which the exchange's recognition would be subject to review by the Commission.[1069] As noted above, DCMs currently exercise discretion with regard to exchange-set limits to approve exemptions meeting the general definition of bona fide hedging position. The Commission works cooperatively with DCMs to enforce compliance with exchange-set speculative position limits. In the 2016 Position Limits Supplemental Proposal, the Commission believed that a continuation of this cooperative process, and an extension to the proposed federal position limits, would be consistent with the policy objectives in CEA section 4a(3)(B).[1070] The Commission is reproposing § 150.9(a)(5), as originally proposed.

d. Proposed § 150.9(a)(6)

*Proposed Rule:* Proposed § 150.9(a)(6) required exchanges that elect to process non-enumerated bona fide hedging position applications to promulgate reporting rules for applicants who own, hold or control positions recognized as non-enumerated bona fide hedging positions. The Commission expected that the exchanges would promulgate enhanced reporting rules in order to obtain sufficient information to conduct an adequate surveillance program to detect and potentially deter excessively large positions that may disrupt the price discovery process. At a minimum, these rules should require applicants to report when an non-enumerated bona fide hedging position has been established, and to update and maintain the accuracy of such reports. These rules should also elicit information from applicants that will assist exchanges in complying with proposed § 150.9(c) regarding exchange reports to the Commission.

*Comments Received:* Several commenters did not support a Commission requirement for additional filings with respect to non-enumerated bona fide hedging positions to be held in the five day/spot month period.[1071] Commenters also requested that the Commission remove the proposed requirement that an exchange must adopt enhanced reporting rules for market participants that rely on exchange recognitions of positions as non-enumerated bona fide hedging positions.[1072] Generally, commenters suggested that any additional reporting requirements be kept simple, streamlined and minimally burdensome.[1073] One commenter expressed the view that the Commission should clarify certain aspects relating to the mechanics and content of proposed reporting requirements for those seeking an exchange-administered hedge exemption.[1074]

*Commission Reproposal:* The Commission has determined to amend and clarify the proposal as follows. First, the Commission clarifies that it does not require additional filings under § 150.9(a)(6); rather, it is in the exchanges' discretion to determine whether there is a reporting requirement for a non-enumerated bona fide hedging position. Consequently, the Commission is amending the regulation text to clarify that exchanges are authorized to, rather than required to, determine whether to require enhanced reporting, providing only that exchanges that determine to process non-enumerated bona fide hedging position applications shall have rules, submitted to the Commission under part 40, that require applicants ''to file reports pertaining to the use of

[1067] Current § 1.47 requires a filing in advance for Commission recognition of a position as a non-enumerated bona fide hedging position.

[1068] *See* 2016 Position Limits Supplemental Proposal discussion regarding proposed § 150.5.

[1069] *See* 2016 Position Limits Supplemental Proposal, nn. 121–123 and accompanying text; *see also* the 2016 Position Limits Supplemental Proposal discussion of proposed § 150.9(d), review of applications by the Commission. Exchange recognition of a position as a non-enumerated bona fide hedging position would allow the market participant to exceed the federal position limit until such time that the Commission notified the market participant to the contrary, pursuant to the proposed review procedure that the exchange action was dismissed. That is, if a party were to hold positions pursuant to a non-enumerated bona fide hedging position recognition granted by the exchange, such positions would not be subject to federal position limits, unless or until the Commission were to determine that such non-enumerated bona fide hedging position recognition is inconsistent with the CEA or CFTC regulations thereunder. Under this framework, the Commission would continue to exercise its authority in this regard by reviewing an exchange's determination and verifying whether the facts and circumstances in respect of a derivative position satisfy the requirements of the Commission's general definition of bona fide hedging position in § 150.1. If the Commission determines that the exchange-granted recognition is inconsistent with section 4a(c) of the Act and the Commission's general definition of bona fide hedging position in § 150.1, a market participant would be required to reduce the derivative position or otherwise come into compliance with position limits within a commercially reasonable amount of time.

[1070] 7 U.S.C. 6a(3)(B).

[1071] CL–IECAssn–60949 at 13; CL–NMPF–60956 at 2; CL–NCFC–60930 at 4–5; CL–ICE–60929 at 22; CL–ICE–60929 at 22; and CL–FIA–60937 at 18, 19.

[1072] *See, e.g.,* CL–FIA–60937 at 15; CL–CMC–60950 at 12–13; CL–CCI–60935 at 7–8; CL–NCGA–NGSA–60919 at 12–13; CL–MGEX–60936 at 6; CL–ISDA–60931 at 10; CL–NGFA–60941 at 4; CL–Working Group–60947 at 12 (footnotes omitted); CL–AMG–60946 at 4–5; CL–CCI–60935 at 7–8; CL–AGA–60943 at 6; CL–CMC–60950 at 12–13; and CL–NCGA–NGSA–60919 at 12–13 (expressing the view that, reporting of positions for non-enumerated bona fide hedges should mirror the mechanism for reporting EBFHs recognized by exchanges that utilize the process where reports of such positions are made to the Commission with an identical copy to be filed with the applicable exchange(s). *See also* CL–MGEX–60936 at 5–6 (requesting that reporting and recordkeeping requirements be removed or at least reduced unless there is a demonstrated need for them and b) only exemptions granted in excess of federal limits should require reporting to the Commission.); and CL–AGA–60943 at 7 (commenting that ''because Exchanges may, at any time, request records of hedgers' cash market and derivative positions or other details and explanations concerning the commercial risks being hedged, any Exchange surveillance function can be met by exchange data inquiries, rather than by an affirmative reporting obligation by a commercial hedger.'').

[1073] CL–NFP–60942 at 6–8); and CL–FIA–60937 at 4, 15.

[1074] CL–CME–60926 at 10.

any such exemption that has been granted in the manner, form, and frequency, as determined by the designated contract market or swap execution facility.''

e. Proposed 150.9(a)(7)—Transparency to Market Participants

*Proposed Rule:* Proposed § 150.9(a)(7) required an exchange to publish on its Web site, no less frequently than quarterly, a description of each new type of derivative position that it recognizes as a non-enumerated bona fide hedge. The Commission envisioned that each description would be an executive summary. The 2016 Position Limits Supplemental Proposal required that the description include a summary describing the type of derivative position and an explanation of why it qualifies as a non-enumerated bona fide hedging position. The Commission believed that the exchanges are in the best position when quickly crafting these descriptions to accommodate an applicant's desire for trading anonymity while promoting fair and open access for market participants to information regarding which positions might be recognized as non-enumerated bona fide hedging positions. The Commission proposed to spot check these summaries pursuant to proposed § 150.9(e).

i. Comments Received

Several commenters proposed that the Commission clarify or confirm that exchanges are not required to divulge confidential information (such as trade secrets, intellectual property, the market participant's identity or position) when providing the summary description of non-enumerated bona fide hedge positions.[1075] One commenter requested ''that the Commission explicitly provide in Rule 150.9(a)(7) that the summaries must be published 'in a manner that preserves the anonymity of the applicant' and provide additional guidance regarding the types of sensitive items that should be omitted from any summary, such as the size of the position(s) taken or to be taken by the applicant or the delivery point(s) or other information that might identify the applicant.'' [1076] Another commenter expressed the view that an exchange should not be required to disclose its own internal analyses when explaining its decision to grant an exemption for a derivative position recognized as a non-enumerated bona fide hedging position.[1077]

*Commission Reproposal:* While the Commission is reproposing the rule, as originally proposed, it clarifies that that any data published pursuant to § 150.9(a)(7) should not disclose the identity of, or confidential information about, the applicant. Rather, any published summaries are expected to be general (generic facts and circumstances) and not include detail that would disclose trade secrets or intellectual property.

f. Proposed § 150.9(a)(8) and Commission Reproposal

Under proposed § 150.9(a)(8), an exchange could elect to request the Commission review a non-enumerated bona fide hedging position application that raises novel or complex issues using the process set forth in proposed § 150.9(d).[1078] If an exchange makes a request pursuant to proposed § 150.9(a)(8), the Commission, as would be the case for an exchange, would not be bound by a time limitation. This is because the Commission proposed only that non-enumerated bona fide hedging position applications be processed in a timely manner.[1079] Essentially, this proposed provision largely preserved the Commission's review process under current § 1.47,[1080] except that a market participant first seeks recognition of a non-enumerated bona fide hedging position from an exchange.

The Commission is reproposing § 150.9(a)(8), as originally proposed.

4. Proposed § 150.9(b)—Recordkeeping Requirements

*Proposed Rule:* Proposed § 150.9(b) outlined the recordkeeping requirements for exchanges that elected to process non-enumerated bona fide hedging position applications under proposed § 150.9(a).[1081] The proposal required that exchanges maintain complete books and records of all activities relating to the processing and disposition of applications in a manner consistent with the Commission's existing general regulations regarding recordkeeping.[1082] In consideration of the fact that DCMs currently recognize non-enumerated bona fide hedging positions which must be updated annually and that the proposal would require annual updates, the Commission proposed that exchanges keep books and records until the termination, maturity, or expiration date of any recognition of a non-enumerated bona fide hedging position and for a period of five years after such date. The Commission stated that five years should provide an adequate time period for Commission reviews, whether that be a review of an exchange's rule enforcement or a review of a market participant's representations.

Exchanges would be required to store and produce records pursuant to current § 1.31 of the Commission's regulations, and would be subject to requests for information pursuant to other applicable Commission regulations including, for example, § 38.5. Consistent with current § 1.31, the Commission clarified its expectation that the records would be readily accessible until the termination, maturity, or expiration date of the recognition and during the first two years of the subsequent five year period. In addition, the Commission did not intend in proposed § 150.9(b)(1) to create any new obligation for an exchange to record conversations with applicants, which includes their representatives; however, the Commission expected that an exchange would preserve any written or electronic notes of verbal interactions with such parties.

Finally, the Commission emphasized that parties who avail themselves of exemptions under § 150.3(a), as proposed in the 2016 Supplemental Position Limits Proposal, would be subject to the recordkeeping requirements of § 150.3(g), as well as

[1075] *See, e.g.,* CL–ICE–60929 at 23; CL–NCGA–NGSA–60919 at 14 (footnote omitted); CL–DFA–60927 at 6; CL–NCFC–60930 at 5; CL–IATP–60951 at 6; CL–EEI–EPSA–60925 at 9; CL–COPE–60932 at 9; CL–DFA–60927 at 6; and CL–NCFC–60930 at 5.

[1076] CL–NCGA–NGSA–60919 at 14 (footnote omitted).

[1077] CL–CME–60926 at 11.

[1078] Under proposed § 150.9(a)(8), if the exchange determines to request that the Commission consider the application, the exchange must, under proposed § 150.9(a)(4)(v)(C), notify an applicant in a timely manner that the exchange has requested that the Commission review the application. This provision provides the exchanges with the ability to request Commission review early in the review process, rather than requiring the exchanges to process the request, make a determination and only then begin the process of Commission review provided for under proposed § 150.9(d). The Commission noted that although most of its reviews would occur after the exchange makes its determination, the Commission could, as provided for in proposed § 150.9(d)(1), initiate its review, in its discretion, at any time.

[1079] Novel facts and circumstances may present particularly complex issues that could benefit from extended consideration, given the Commission's current resource constraints.

[1080] 17 CFR 1.47.

[1081] *Id.* Proposed § 150.10(b) and § 150.11(b) contain substantially similar recordkeeping requirements regarding spread exemptions and anticipatory hedge exemptions.

[1082] Requirements regarding the keeping and inspection of all books and records required to be kept by the Act or the Commission's regulations are found at § 1.31, 17 CFR 1.31. DCMs and SEFs are already required to maintain records of their business activities in accordance with the requirements of § 1.31 and 17 CFR 38.951. *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38474 (providing a more comprehensive discussion of proposed § 150.9(b)).

requests from the Commission for additional information under § 150.3(h), as each was proposed in the December 2013 Position Limits Proposal. The Commission noted that it might request additional information, for example, in connection with review of an application.[1083]

*Commission Reproposal:* The Commission did not receive comments on § 150.9(b) (nor on § 150.10(b) or § 150.11(b)), and is reproposing § 150.9(b), as originally proposed, for the reasons explained in the 2016 Supplemental Position Limits Proposal.[1084]

5. Proposed § 150.9(c)—Exchange Reporting

*Proposed Rule:* Proposed § 150.9(c)(1) required an exchange that elected to process non-enumerated bona fide hedge applications to submit a weekly report to the Commission.[1085] The proposed report would provide information regarding each commodity derivative position recognized by the exchange as a non-enumerated bona fide hedging position during the course of the week. Information provided in the report would include the identity of the applicant seeking such an exemption, the maximum size of the derivative position that was recognized by the exchange as a non-enumerated bona fide hedging position,[1086] and, to the extent that the exchange determined to limit the size of such bona fide hedging position under the exchange's own speculative position limits program, the size of any limit established by the exchange.

The Commission envisioned that the proposed report would specify the maximum size and/or size limitations by contract month and/or type of limit (*e.g.,* spot month, single month, or all-months-combined), as applicable.[1087] The proposed report would also provide information regarding any revocation of, or modification to the terms and conditions of, a prior determination by the exchange to recognize a commodity derivative position as a non-enumerated bona fide hedge. In addition, the report would include any summary of a type of recognized non-enumerated bona fide hedge that was, during the course of the week, published or revised on the exchange's Web site pursuant to proposed § 150.9(a)(7).

The Commission noted that the proposed weekly report would support its surveillance program by facilitating the tracking of non-enumerated bona fide hedges recognized by exchanges,[1088] keeping the Commission informed of the manner in which an exchange was administering its procedures for recognizing such positions. For example, the report would make available to the Commission, on a regular basis, the summaries of types of recognized non-enumerated bona fide hedges that an exchange posts to its Web site pursuant to proposed § 150.9(a)(7). This would facilitate any review by the Commission of such summaries, pursuant to proposed § 150.9(e), and would help to ensure, if the Commission determines that revisions to a summary are necessary, that such revisions were carried out in a timely manner by the exchange.

The Commission noted that in certain instances, information included in the proposed weekly report could prompt the Commission to request records required to be maintained by an exchange pursuant to proposed § 150.9(b).[1089] The 2016 Supplemental Position Limit Proposal clarified that it was the Commission's expectation that the summary would focus on the facts and circumstances upon which an exchange based its determination to recognize a commodity derivative position as a non-enumerated bona fide hedging position, or to revoke or modify such recognition. The Commission also noted that it might decide, in light of the information provided in the summary, or any other information included in the proposed weekly report regarding the position, that it should request the exchange's complete record of the application for recognition of the position as an non-enumerated bona fide hedge—in order to determine, for example, whether the application presents novel or complex issues that merit additional analysis pursuant to proposed § 150.9(d)(2), or to evaluate whether the disposition of the application by the exchange was consistent with section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1.

In addition, proposed 150.9(c)(2) required an exchange to submit to the Commission any report made to the exchange by an applicant, pursuant to proposed § 150.9(a)(6), that notified the exchange that the applicant owned or controlled a commodity derivative position that the exchange had recognized as an non-enumerated bona fide hedging position, at least monthly,[1090] unless otherwise instructed by the Commission.[1091] The exchange's submission of these reports would notify the Commission that an applicant had taken a commodity derivative position recognized by the exchange as a non-enumerated bona fide hedging position, and would also show the applicant's offsetting positions in the cash markets. Requiring an exchange to submit these reports to the Commission would therefore support

[1083] The Commission pointed out that in the December 2013 Position Limits Proposal, persons claiming exemptions under proposed § 150.3 must still "maintain complete books and records concerning all details of their related cash, forward, futures, options and swap positions and transactions. Furthermore, such persons must make such books and records available to the Commission upon request under proposed § 150.3(h), which would preserve the 'special call' rule set forth in current 17 CFR 150.3(b)." 78 FR 75741 (footnote omitted).

[1084] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38474.

[1085] *Id.*

[1086] The Commission noted that an exchange could determine to recognize all, or a portion, of the commodity derivative position in respect of which an application for recognition had been submitted, as a non-enumerated bona fide hedging position, provided that such determination was made in accordance with the requirements of proposed § 150.9 and was consistent with the Act and the Commission's regulations. *Id.*

[1087] Under the proposal, an exchange could determine to recognize all, or a portion, of the commodity derivative position in respect of which an application for recognition has been submitted, as an non-enumerated bona fide hedge, for different contract months or different types of limits (*e.g.,* a separate limit level for the spot month). *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38474.

[1088] The Commission stated that the exchange's assignment of a unique identifier to each of the non-enumerated bona fide hedge applications that the exchange received, and, separately, the exchange's assignment of a unique identifier to each type of commodity derivative position that the exchange recognized as a non-enumerated bona fide hedge, would assist the Commission's tracking process. Accordingly, the Commission suggested that, as a "best practice," the exchange's procedures for processing non-enumerated bona fide hedge applications contemplate the assignment of such unique identifiers. The Commission noted that under proposed § 150.9(c)(1)(i), an exchange that assigned such unique identifiers would be required to include the identifiers in the exchange's weekly report to the Commission.

[1089] For example, as proposed, for each derivative position recognized by the exchange as a non-enumerated bona fide hedge, or any revocation or modification of such recognition, the report would include a concise summary of the applicant's activity in the cash markets for the commodity underlying the position.

[1090] As proposed, the timeframe within which an applicant would be required to report to the exchange would be established by the exchange in its rules, as appropriate and in accordance with proposed § 150.9(a)(6). The Commission also pointed out that an exchange could decide to require such reports from its participants more frequently than monthly.

[1091] As proposed, under § 150.9(f)(1)(ii), the Commission would delegate to the Director of the Commission's Division of Market Oversight, or such other employee or employees as the Director designated from time to time, the authority to provide instructions regarding the submission to the Commission of information required to be reported by an exchange pursuant to proposed § 150.9(c). *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38475.

the Commission's surveillance program, by facilitating the tracking of non-enumerated bona fide hedging positions recognized by the exchange, and helping the Commission to ensure that an applicant's activities conform to the terms of recognition that the exchange had established.

Proposed § 150.9(c)(3)(i) and (ii) would require an exchange, unless instructed otherwise by the Commission, to submit weekly reports under proposed § 150.9(c)(1), and applicant reports under proposed § 150.9(c)(2). Proposed § 150.9(c)(3)(i) and (ii) contemplated that, in order to facilitate the processing of such reports, and the analysis of the information contained therein, the Commission would establish reporting and transmission standards, and that it may require reports to be submitted to the Commission using an electronic data format, coding structure and electronic data transmission procedures approved in writing by the Commission, as specified on the Forms and Submissions page at *www.cftc.gov.*[1092] Proposed § 150.9(c)(3)(iii) would require such reports to be submitted to the Commission no later than 9:00 a.m. Eastern time on the third business day following the report date, unless the exchange was otherwise instructed by the Commission.[1093]

*Comments Received:* Several commenters expressed views against the § 150.9(c) reporting requirements, or requested that the Commission reduce or alter the reporting requirements for exchanges.[1094] One commenter requested that the Commission clarify that proposed weekly reporting requirements for exchanges only require reporting of the ''most essential information'' regarding exchange-administered hedge exemptions.[1095] As an alternative to the entire proposed exchange-administered exemption reporting requirements, one commenter proposed that exchanges provide a weekly report to the Commission summarizing newly approved hedge exemptions.[1096]

*Commission Reproposal:* The Commission is reproposing the rule, largely as originally proposed, except that the Commission has revised §§ 150.9(c)(1)(i) and 150.9(c)(2) for purposes of clarification. In regards to § 150.9(c)(1)(i), the Commission is clarifying that the reports required under (c)(1)(i) are those for each commodity derivatives position that had been recognized that week and for any revocation or modification of a previously granted recognition. As to § 150.9(c)(2), in response to commenters, the Commission clarifies that exchanges are authorized under § 150.9(c)(2), but are not required, to determine whether to incorporate additional reporting requirements in connection with its recognition of non-enumerated bona fide hedging positions. If an exchange does determine to require additional reporting, § 150.9(c)(2) requires that the exchange submit reports no less frequently than monthly.[1097] In addition, the Commission believes the weekly reporting requires only the most essential information regarding exchange-administered exemptions.

6. Proposed § 150.9(d)—Review of Applications by the Commission

*Proposed Rule:* Proposed § 150.9(d) provided for Commission review of applications to ensure that the processes administered by the exchange, as well as the results of such processes, were consistent with the requirements of section 4a(c) of the Act and the Commission's regulations thereunder.[1098] The Commission proposed to review records required to be maintained by an exchange pursuant to proposed § 150.9(b); however, under the proposal the Commission could request additional information under proposed § 150.9(d)(1)(ii) if, for example, the Commission found additional information was needed for its own review.

Under the proposal, the Commission could decide to review a pending application prior to disposition by an exchange, but anticipated that it would most likely wait to review applications until after some action has already been taken by an exchange. As proposed, § 150.9(d)(2) and (3) would require the Commission to notify the exchange and applicable applicant that they had 10 business days from the date of the request to provide any supplemental information. The Commission noted that this approach provided the exchanges and the particular market participant with an opportunity to respond to any issues raised by the Commission.

During the period of any Commission review of an application, an applicant could continue to rely upon any recognition previously granted by the exchange. If the Commission determined that remediation was necessary, the Commission would provide for a commercially reasonable amount of time for the market participant to comply with limits after announcement of the Commission's decision under proposed § 150.9(d)(4).[1099] In determining a time, the Commission could consider factors such as current market conditions and the protection of price discovery in the market. Proposed § 150.10(d) and § 150.11(d) contain substantially similar requirements regarding review of applications by the Commission of

[1092] The delegation proposed in § 150.9(f)(1)(ii) would also, in connection with proposed § 150.9(c)(3), delegate to the Director of the Commission's Division of Market Oversight, or such other employee or employees as the Director designated from time to time, the authority: (i) To provide instructions for the proposed submissions; and (ii) to specify on the Forms and Submissions page at *www.cftc.gov* the manner for submitting to the Commission information required to be reported by an exchange pursuant to proposed § 150.9(c), and to determine the format, coding structure and electronic data transmission procedures for submitting such information. *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38475.

[1093] For purposes of proposed § 150.9(c)(2), the timeframe set forth in proposed § 150.9(c)(3)(iii) would be calculated from the date of a exchange's submission to the Commission, and not from the date of an applicant's report to the exchange.

[1094] CL–AMG–60946 at 3; CL–CME–60926 at 11; CL–ICE–60929 at 8–9 and 16; and CL–CMC–60950 at 13–14.

[1095] CL–CME–60926 at 11.

[1096] CL–ICE–60929 at 8–9 and 16.

[1097] As reproposed, § 150.9(c)(2) also provides that instead of submitting any such reports monthly, the Commission could otherwise instruct the exchange otherwise.

[1098] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38475–76. As the proposal noted, the Commission agreed with the comment of one participant at the June 19, 2014 Roundtable on Position Limits, who said that if the Commission were to permit exchanges to administer a process for non-enumerated bona fide hedging positions, the Commission should continue to do ''a certain amount of de novo analysis and review.'' *Id.*

The Commission noted that, under the proposal, the SRO's recognition was tentative, because the Commission would reserve the power to review the recognition, subject to the reasonably fixed statutory standards in CEA section 4a(c)(2) (directing the CFTC to define the term bona fide hedging position) that are incorporated into the Commission's proposed general definition of bona fide hedging position in § 150.1. The SRO's recognition would also be constrained by the SRO's rules, which would be subject to CFTC review under the proposal. The Commission pointed out that SROs are parties subject to Commission authority, their rules are subject to Commission review and their actions are subject to Commission de novo review under the proposal—SRO rules and actions may be changed by the Commission at any time. In addition, the Commission noted that under the proposal, the exchange was required to make its determination consistent with both CEA section 4a(c) and the Commission's general definition of bona fide hedging position in § 150.1. Further, the Commission noted that CEA section 4a(c)(1) requires a position to be shown to be bona fide as defined by the Commission.

[1099] The Commission noted a commercially reasonable time period as necessary to exit the market in an orderly manner, generally, ''would be less than one business day.'' 2016 Supplemental Position Limits Proposal, 81 FR at 38476, n. 168 (citing the December 2013 Position Limits Proposal, 78 FR at 75713).

spread exemptions and anticipatory hedge exemptions.

*Comments Received:* Several commenters were concerned about the Commission review process and/or provided suggestions on how the Commission should modify or limit its authority to review exchange-granted exemptions.[1100]

One commenter requested that the Commission define in more detail, in the final rule, how this review process will work.[1101] Another commenter recommended that exemptions granted by an exchange be given deference by the Commission upon subsequent review, with reversal occurring only when there is evidence of negligence or abuse, or when it may lead to market disruption.[1102] Four commenters suggested that the Commission limit the time available for it to review a non-enumerated bona fide hedging position exemption granted by an exchange in an effort to provide regulatory certainty to entities relying on that exemption.[1103] Fourteen commenters expressed the view that a ''commercially reasonable'' amount of time for an entity to unwind its position should not be limited to one business day or less. Instead, these commenters advocated that the Commission or the exchange should determine how long an entity has to unwind a position given the facts and circumstances of each situation.[1104] Three commenters expressed the view that when the Commission reviews and affirms a non-enumerated bona fide hedging position determination, such a determination should result in a new enumerated bona fide hedging position.[1105]

Some commenters opined that the Commission should instead explicitly require Commission review and approval of all hedge exemption requests received by an exchange.[1106] These commenters believe that the Commission should always make the final decision regarding whether to grant a particular hedge exemption.

*Commission Reproposal:* After carefully considering the comments received, the Commission is reproposing § 150.9(d), as originally proposed. The Commission believes the proposed de novo review of exchange-granted non-enumerated bona fide hedging position exemptions is adequate to maintain proper exchange oversight and to verify that such exemptions provide fair and open access by all market participants. Further, the Commission notes that it must maintain de novo review on a case-by-case basis; otherwise, as discussed above, the exchange exemption process may be considered an illegal delegation of Commission authority to exchanges.[1107]

Regarding the recommendation that the Commission limit its available time to review exchange granted exemptions, this limitation may appear inconsistent with case law regarding authorizations for self-regulatory organizations to make determinations, subject to de novo agency review.[1108] Regarding whether the Commission would expose exchanges to undue regulatory penalties or uncertainty for exemptions the Commission overturns, the Commission declines to speculate on any actions that it may take, beyond the notice to the applicant. Regarding giving entities a ''commercially reasonable'' time for an entity to unwind their positions, the Commission has not proposed a fixed time period, but would consider the facts and circumstances of each situation.

In response to comments that the Commission should create a new enumerated hedge for any non-enumerated bona fide hedging position determination the Commission reviews and affirms, the Commission clarifies that under the de novo review standard, no deference is provided to a prior determination; rather, the Commission will review as if no decision has been previously made. This is the same as a ''hearing de novo.'' [1109] The Commission also notes that, as previously discussed, an exchange can petition under § 13.2 for Commission recognition of a generic position as an enumerated bona fide hedging position, and that market participants have the flexibility of two processes for recognition of a position as an enumerated bona fide hedging position: (i) Request an exemptive, no-action or interpretative letter under § 140.99; and/or (ii) petition under § 13.2 for changes to Appendix B to part 150.

The reproposed rule is confined to federal limits and does not interfere with existing exemption processes that exchanges currently implement and oversee with regard to exchange-set limits. Exchanges remain bound by the bona fide hedging position definition in this part for any recognition for purposes of federal limits. But, as noted above, in regards to reproposed § 150.9(a), exchange processes for exchange-set limits that are lower than the federal limit could differ as long as

[1100] CL–CMC–60950 at 14; CL–NFP–60942 at 6–8; CL–DFA–60927 at 1–2; CL–ICE–60929 at 5–8; CL–ISDA–60931 at 6–7; CL–AGA–60943 at 7; CL–FIA–60937 at 2, 6, 7; CL–COPE–60932 at 7; CL–COPE–60932 at 7–8; CL–EEI–EPSA–60925 at 10–11; CL–RER2–60962 at 1; CL–Public Citizen–60940 at 2; and CL–MGEX–60936 at 7. *See also* CL–FIA–60937 at 7, 8; CL–COPE–60932 at 7; CL–NGFA–60941 at 3; CL–ICE–60929 at 18; CL–API–60939 at 4; CL–EEI–EPSA–60925 at 10–11; CL–IECAssn–60949 at 9–10 (recommending for an appeals process and/or notice and public comment feature for the Commission review process); CL–FIA–60937 at 7, 8 (recommending that market participants have continued reliance on any overturned exemption for one year after the overturn or modification); CL–NGFA–60941 at 3 (suggesting that a vote by the full Commission should be required on the ''weighty decision'' to invalidate a hedge exemption after thorough analysis and careful consideration); and CL–MGEX–60936 at 7 (expressing concerns that there is legal uncertainty and lack of clarity in how the non-enumerated bona fide hedging position process will work).

[1101] CL–AFIA–60955 at 2.

[1102] CL–MGEX–60936 at 7–8.

[1103] CL–FIA–60937 at 3; CL–ICE–60929 at 18; CL–API–60939 at 4; and CL–API–60939 at 1. *See also* CL–API–60939 at 1 (requesting that, if the Commission conducts a review of an exchange granted non-enumerated bona fide hedging position exemption, then the Commission should limit the time period to 180 days to issue a decision to overturn an exemption); CL–AGA–60943 at 8 (suggesting that the Commission ''should adopt a rule that follows its current approach under CFTC Rule 1.47); CL–IECAssn–60949 at 11–12 (recommending a reasonable time period to unwind positions for which an exemption has been overturned would help to allow the market to operate smoothly); and CL–FIA–60937 at 7 (noting that the Commission should ''require an exchange to post a general description of a non-enumerated hedge, spread, or anticipatory hedge exemption on its Web site within 30 days of granting the exemption,'' and thereafter, ''the Commission should have 180 days to decide whether to review and overturn or modify an exemption posted on an exchange's Web site.'').

[1104] *See, e.g.,* CL–API–60939 at 4; CL–FIA–60937 at 3, 8; CL–MGEX–60936 at 7–8; CL–ISDA–60931 at 7; CL–NGFA–60941 at 3; CL–NFP–60942 at 8; CL–AGA–60943 at 2; CL–AGA–60943 at 7; CL–AMG–60946 at 5; CL–ICE–60929 at 18; CL–CMC–60950 at 11; CL–NCGA–NGSA–60919 at 13; CL–EEI–EPSA–60925 at 10; and CL–ISDA–60931 at 7. *See also* CL–FIA–60937 at 3, 8 (recommending the Commission consider ''(1) the size of, and risks associated with, the participant's cash and related derivative positions; (2) the risks created by the need to reduce what will become an un-hedged cash market exposure; and (3) the availability of sufficient liquidity to enable the market participant to reduce the hedging and the underlying positions without incurring losses solely as a result of being forced to liquidate the hedge within a constrained timeframe.'').

[1105] CL–COPE–60932 at 7; CL–EEI–EPSA–60925 at 11; and CL–COPE–60932 at 7.

[1106] CL–Public Citizen–60940 at 2; and CL–RER2–60962 at 1.

[1107] *See also* 2016 Supplemental Position Limits Proposal, 81 FR at38464–66 (discussing the Commission's authority to permit certain exchanges to recognize positions as bona fide hedging positions for purposes of federal limits, as well as the careful provisions proposed in § 150.9 to do so within the limitations on its authority).

[1108] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38465, n. 83. The recommendation might also unduly constrain agency resources.

[1109] *See* Black's Law Dictionary 837 (10th ed. 2014) (defining ''hearing de novo'' as ''[a] reviewing court's decision of a matter anew, giving no deference to a lower court's findings. A new hearing of a matter, conducted as if the original hearing had not taken place.'').

the exemption provided by the exchange is capped at the level of the applicable federal limit in § 150.2.

Regarding requests to revise the Commission's review process (*i.e.,* include an appeals process, provide notice and public comment opportunity, require a vote by the Commission to overturn an exchange-granted exemption, provide more detail on the review process), the Commission notes that it has not proposed to delegate authority to staff to overturn an exchange determination.

7. Proposed § 150.9(e)—Review of summaries by the Commission

*Proposed Rule:* In connection with proposed § 150.9(a)(7), for the Commission to rely on the expertise of the exchanges to summarize and post executive summaries of non-enumerated bona fide hedging positions to their respective Web sites, the Commission proposed, in § 150.9(e), to review such executive summaries to ensure the summaries provided adequate disclosure to market participants of the potential availability of relief from speculative position limits. The Commission stated that it believed an adequate disclosure would include generic facts and circumstances sufficient to alert similarly situated market participants to the possibility of receiving recognition of a non-enumerated bona fide hedging position. Such market participants could then use that information to help evaluate whether to apply for recognition of a non-enumerated bona fide hedging position. Thus, the Commission noted, adequate disclosure should help ensure fair and open access to the application process. Due to resource constraints, the Commission pointed out that it might not be able to preclear each summary, so it proposed to spot check executive summaries after the fact.

Commission Reproposal

The Commission did not receive comments on § 150.9(e) (nor on § 150.10(e)), and is reproposing § 150.9(e), as originally proposed, for the reasons explained in the 2016 Supplemental Position Limits Proposal.[1110]

8. Proposed § 150.9(f)—Delegation of Authority

Proposed Rule

The Commission proposed to delegate certain of its authorities under proposed § 150.9 (and § 150.10 and § 150.11), to the Director of the Commission's Division of Market Oversight, or such other employee or employees as the Director designated from time to time. In § 150.9(f), the Commission proposed to delegate, until it ordered otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director designated from time to time, the authorities under certain parts of §§ 150.9(a); 150.9(c); 150.9(d); and 150.9(e). As noted, similar delegations were contained in proposed § 150.10(f) and § 150.11(e) for spread exemptions and enumerated anticipatory hedge exemptions, respectively.

Proposed § 150.9(f)(1)(i), § 150.10(f)(1)(i) and § 150.11(e)(1)(i) delegated the Commission's authority to the Division of Market Oversight to provide instructions regarding the submission of information required to be reported to the Commission by an exchange, and to specify the manner and determine the format, coding structure, and electronic data transmission procedures for submitting such information. Proposed § 150.9(f)(1)(v) and § 150.10(f)(1)(v) delegated the Commission's review authority under proposed § 150.9(e) and § 150.10(e), respectively, to DMO with respect to summaries of types of recognized non-enumerated bona fide hedging positions, and types of spread exemptions, that were required to be posted on an exchange's Web site pursuant to proposed § 150.9(a)(7) and § 150.10(a)(7), respectively.

Proposed § 150.9(f)(1)(i), § 150.10(f)(1)(i) and § 150.11(e)(1)(i) delegated the Commission's authority to the Division of Market Oversight to agree to or reject a request by an exchange to consider an application for recognition of an non-enumerated bona fide hedging position or enumerated anticipatory bona fide hedging position, or an application for a spread exemption. Proposed § 150.9(f)(1)(iii), § 150.10(f)(1)(iii) and § 150.11(e)(1)(iii) delegated the Commission's authority to review any application for recognition of a non-enumerated bona fide hedging position or enumerated anticipatory bona fide hedging position, or application for a spread exemption, and all records required to be maintained by an exchange in connection with such application. Proposed § 150.9(f)(1)(iii), § 150.10(f)(1)(iii) and § 150.11(e)(1)(iii) also delegated the Commission's authority to request such records, and to request additional information in connection with such application from the exchange or from the applicant.

Proposed § 150.9(f)(1)(iv) and § 150.10(f)(1)(iv) delegated the Commission's authority, under proposed § 150.9(d)(2) and § 150.10(d)(2), respectively, to determine that an application for recognition of an non-enumerated bona fide hedging position, or an application for a spread exemption, required additional analysis or review, and to provide notice to the exchange and the particular applicant that they had 10 days to supplement such application.

The Commission did not propose to delegate its authority under proposed § 150.9(d)(3) or § 150.10(d)(3) to make a final determination as to the exchange's disposition. The Commission stated that if an exchange's disposition raised concerns regarding consistency with the Act or presents novel or complex issues, then the Commission should make the final determination, after taking into consideration any supplemental information provided by the exchange or the applicant.[1111]

Comments Received

One commenter recommended that the Commission clarify the delegation provisions referenced in RFC 31 by expressly stating that ''the Commission, not DMO, now and always will retain the ultimate authority to grant or deny Exemption applications.''[1112]

Commission Reproposal

The Commission is reproposing the delegation provisions, as originally proposed. With regard to the comment received, the Commission notes that, as provided in both proposed and reproposed § 150.9(f)(3), it retains the authority to make the final determination to grant or deny hedge exemption applications submitted pursuant to this rulemaking. However, the Commission also points out that any decisions of an existing Commission under this rulemaking cannot effectively bind a future commission, since such future Commission could amend or revoke such a rule.

*H. § 150.10—Process for Designated Contract Market or Swap Execution Facility Exemption From Position Limits for Certain Spread Positions*

1. Background 150.10

In the 2016 Supplemental Position Limits Proposal, the Commission proposed to permit exchanges, by rule, to exempt from federal position limits certain spread transactions, as authorized by CEA section 4a(a)(1),[1113]

[1110] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38476.

[1111] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38482.

[1112] CL–Working Group–60947 at 22.

[1113] 7 U.S.C. 6a(a)(1) (authorizing the Commission to exempt transactions normally known to the trade as ''spreads''). DCMs currently process applications and in light of the provisions of CEA section 4a(a)(3)(B) and CEA section 4a(c)(2)(B).[1114] In particular, CEA section 4a(a)(1) provides the Commission with authority to exempt from position limits transactions normally known to the trade as ''spreads'' or ''straddles'' or ''arbitrage'' or to fix limits for such transactions or positions different from limits fixed for other transactions or positions. The Commission noted that the Dodd-Frank Act amended the CEA by adding section 4a(a)(3)(B), which now directs the Commission, in establishing position limits, to ensure, to the maximum extent practicable and in its discretion, ''sufficient market liquidity for bona fide hedgers.'' [1115] The Commission also noted that the Dodd-Frank Act amendments to the CEA in section 4a(c)(2)(B) limited the definition of a bona fide hedging position regarding positions (in addition to those included under CEA section 4a(c)(2)(A)) [1116] resulting from a swap that was executed opposite a counterparty for which the transaction would qualify as a bona fide hedging transaction, in the event the party to the swap is not itself using the swap as a bona fide hedging transaction. In this regard, the Commission interpreted this statutory definition to preclude spread exemptions for a swap position that was executed opposite a counterparty for which the transaction would *not* qualify as a bona fide hedging transaction.

As noted in the 2016 Supplemental Position Limits Proposal, prior to the passage of the Dodd-Frank Act, the Commission exercised its exemptive authority pertaining to spread transactions in promulgating current § 150.3. Current § 150.3 provides that the position limits set in § 150.2 may be exceeded to the extent such positions are spread or arbitrage positions between single months of a futures contract and/or, on a futures-equivalent basis, options thereon, outside of the spot month, in the same crop year; provided, however, that such spread or arbitrage positions, when combined with any other net positions in the single month, do not exceed the all-months limit set forth in § 150.2. In addition, the Commission has permitted DCMs, in setting their own position limits under the terms of current § 150.5(a), to exempt spread, straddle or arbitrage positions or to fix limits that apply to such positions that are different from limits fixed for other positions.[1117]

Under the December 2013 Position Limits Proposal, the exemption in current § 150.3(a)(3) for spread or arbitrage positions between single months of a futures contract or options thereon, outside the spot month would be deleted. As the Commission noted, the proposal would instead maintain the current practice in § 150.2 of setting single-month limits at the same levels as all-months limits, which would render the ''spread'' exemption unnecessary.[1118] In particular, the spread exemption set forth in current § 150.3(a)(3) permits a spread trader to exceed single month limits only to the extent of the all months limit. Because the Commission, in current § 150.2 and as proposed in the December 2013 Position Limits Proposal, sets single month limits at the same level as all months limits, the existing spread exemption would no longer provide useful relief.

The Commission also noted that the December 2013 Position Limits Proposal would codify guidance in proposed § 150.5(a)(2)(ii) to allow an exchange to grant exemptions from exchange-set position limits for intramarket and intermarket spread positions (as those terms were defined in proposed § 150.1) involving commodity derivative contracts subject to the federal limits. To be eligible for the exemption in proposed § 150.5(a)(2)(ii), intermarket and intramarket spread positions, under the December 2013 Position Limits Proposal, would have to be outside of the spot month for physical delivery contracts, and intramarket spread positions could not exceed the federal all-months limit when combined with any other net positions in the single month. As proposed in the December 2013 Position Limits Proposal, § 150.5(a)(2)(iii) would require traders to apply to the exchange for any exemption, including spread exemptions, from its speculative position limit rules.

Several commenters responding to the December 2013 Position Limits Proposal requested that the Commission provide a spread exemption to federal position limits.[1119] Most of these commenters urged the Commission to recognize spread exemptions in the spot month as well as non-spot months.[1120] Several of these commenters noted that the Commission's proposal would permit exchanges to grant spread exemptions for exchange-set limits in commodity derivative contracts subject to federal limits, and recommended that the Commission establish a process for granting such spread exemptions for purposes of Federal limits.[1121]

In response to these comments, the Commission proposed in its 2016 Supplemental Position Limits Proposal [1122] to permit exchanges to process and grant applications for spread exemptions from federal position limits. At that time, the Commission noted that most, if not all, DCMs already have rules in place to process and grant applications for spread exemptions from exchange-set position limits pursuant to part 38 of the Commission's regulations (in particular, current §§ 38.300 and 38.301) and current § 150.5. And, as noted above, the Commission pointed out that it has a long history of overseeing the performance of the DCMs in granting spread exemptions under current exchange rules regarding exchange-set position limits and believed that it would be efficient, and in the best interest of the markets, in light of current resource constraints, to rely on the exchanges to process applications for spread exemptions from federal position limits. In addition, the

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for exemptions from exchange-set position limits for certain spread positions pursuant to CFMA-era regulatory parameters. *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38467, n. 101.

The Commission pointed out that, in current § 150.3(a)(3), the Commission exempts spread positions ''between single months of a futures contract and/or, on a futures-equivalent basis, options thereon, outside of the spread month, in the same crop year,'' subject to certain limitations. 17 CFR 150.3(a)(3).

[1114] 7 U.S.C. 6a(a)(3)(B) and 7 U.S.C. 6a(c)(2)(B), respectively.

[1115] CEA section 4a(a)(3)(B) also directs the Commission, in establishing position limits, to diminish, eliminate, or prevent excessive speculation; to deter and prevent market manipulation, squeezes, and corners; and to ensure that the price discovery function of the underlying market is not disrupted.

[1116] 7 U.S.C. 6a(c)(2)(A). As explained in the 2016 Supplemental Position Limits Proposal, 81 FR at 38464, n. 66, CEA section 4a(c)(2) generally requires the Commission to define a bona fide hedging position as a position that in CEA section 4a(c)(2)(A): Meets three tests (a position (1) is a substitute for activity in the physical marketing channel, (2) is economically appropriate to the reduction of risk, and (3) arises from the potential change in value of current or anticipated assets, liabilities or services); or, in CEA section 4a(c)(2)(B), reduces the risk of a swap that was executed opposite a counterparty for which such swap would meet the three tests.

[1117] Current § 150.5 applies as non-exclusive guidance and acceptable practices for compliance with DCM core principle 5. *See* December 2013 Position Limits Proposal, 78 FR at 75750–2; *see also* 2016 Supplemental Position Limits Proposal, 81 FR at 38477, n. 173.

[1118] *See* December 2013 Position Limits Proposal, 78 FR at 75736; *see also* 2016 Supplemental Position Limits Proposal, 81 FR at 38477.

[1119] *See, e.g.,* CL–CMC–59634 at 15; CL–Olam–59658 at 7; CL–CME–59718 at 69–71; CL–Citadel–59717 at 8, 9; CL–Armajaro–59729 at 2; and CL–ICEUS–59645 at 8–10.

[1120] *See* CL–CMC–59634 at 15; CL–Olam–59658 at 7; CL–CME–59718 at 71; CL–Armajaro–59729 at 2; and CL–ICEUS–59645 at 8–10.

[1121] *See* CL–Olam–59658 at 7; CL–CME–59718 at 71; CL–ICEUS–59645 at 10.

[1122] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38476–80.

Commission stated that, because many market participants may be familiar with current DCM practices regarding spread exemptions, permitting DCMs to build on current practice may lower the burden on market participants and reduce duplicative filings at the exchanges and the Commission. The 2016 Supplemental Position Limits Proposal noted that this plan would permit exchanges to provide market participants with spread exemptions, pursuant to exchange rules submitted to the Commission; however, the Commission also pointed out that it would retain the authority to review—and, if necessary, reverse—the exchanges' actions.[1123]

Proposed § 150.10 and the public comments relevant to each proposed subsection are discussed below.

2. Discussion

As discussed in greater detail below, the Commission is reproposing § 150.10, largely as originally proposed. Some changes were made in response to concerns raised by commenters; other changes conform to changes made in § 150.9 or § 150.11. Finally, several non-substantive changes were made in response to commenter questions to provide greater clarity.

a. Proposed § 150.10(a)(1)

Proposed Rule

The Commission contemplated in proposed § 150.10(a)(1) that exchanges could voluntarily elect to process spread exemption applications, by filing new rules or rule amendments with the Commission pursuant to part 40 of the Commission's regulations.[1124] The process proposed under § 150.10(a) was substantially similar to that described above for proposed § 150.9(a). For example, proposed § 150.10(a)(1) provided that, with respect to a commodity derivative position for which an exchange elected to process spread exemption applications, (i) the exchange must list for trading at least one component of the spread or must list for trading at least one contract that is a referenced contract included in at least one component of the spread; and (ii) any such exchange contract must be actively traded and subject to position limits for at least one year on that exchange. As noted with respect to the process outlined above for proposed § 150.9(a), the Commission expressed its belief that that an exchange should process spread exemptions only if it had at least one year of experience overseeing exchange-set position limits in an actively traded referenced contract that was in the same commodity as that of at least one component of the spread. The Commission stated that an exchange may not be familiar enough with the specific needs and differing practices of the participants in those markets for which an individual exchange did not list any actively traded referenced contract in a particular commodity. If a component of a spread was not actively traded on an exchange that elected to process spread exemption applications, such exchange might not be incentivized to protect or manage the relevant commodity market, and the interests of such exchange might not be aligned with the policy objectives of the Commission as expressed in CEA section 4a(a)(3)(B). The Commission expected that an individual exchange would describe how it would determine whether a particular component of a spread was actively traded in its rule submission, based on its familiarity with the specific needs and differing practices of the participants in the relevant market.

Consistent with the restrictions regarding the offset of risks arising from a swap position in CEA section 4a(c)(2)(B), proposed § 150.10(a)(1) would not permit an exchange to recognize a spread between a commodity index contract and one or more referenced contracts. That is, an exchange could not grant a spread exemption where a bona fide hedging position could not be recognized for a pass through swap offset of a commodity index contract.[1125]

The Commission noted that for inter-commodity spreads in which different components of the spread were traded on different exchanges, the exemption granted by one exchange would be recognized by the Commission as an exemption from federal limits for the applicable referenced contract(s), but would not bind the exchange(s) that listed the other components of the spread to recognize the exemption for purposes of that other exchange(s)' position limits. In such cases, a trader seeking such inter-commodity spread exemptions would need to apply separately for a spread exemption from each exchange-set position limit.

Comments Received

Two commenters recommended that the Commission should, to the greatest extent possible, allow the exchanges to administer exemptions for non-enumerated bona fide hedging positions, enumerated bona fide hedges, and spread positions in the same manner as they have been to date and allow exchanges to continue to independently evaluate exemption applications by relying on the exchange's extensive knowledge of the markets.[1126]

Five commenters recommended that the Commission not adopt the ''active trading'' and ''one year experience'' requirements as proposed in the supplement regarding a DCM's qualification to administer exemptions from federal position limits.[1127] For a more detailed discussion please see § 150.9(a)(1) above.

Alternatively, several commenters expressed views against the

[1123] 2016 Supplemental Position Limits Proposal, 81 FR at 38477.

[1124] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38464, n. 63, regarding Commission authority to recognize spreads under CEA section 4a(a)(1). Any action of the exchange to recognize a spread, pursuant to rules filed with the Commission, would be subject to review and revocation by the Commission.

[1125] The Commission's interprets CEA section 4a(c)(2)(b) is a mandate from Congress to narrow the scope of what constitutes a bona fide hedging position in the context of index trading activities. ''Financial products are not substitutes for positions taken or to be taken in a physical marketing channel. Thus, the offset of financial risks from financial products is inconsistent with the proposed definition of bona fide hedging for physical commodities.'' *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38471; *see also* December 2013 Position Limits Proposal, 78 FR at 75740. *See also* the discussion of the temporary substitute test. *Id.* at 75708–9.

[1126] CL–NCGA–NGSA–60919 at 9 and CL–IECAssn–60949 at 3–4.

[1127] *See, e.g.,* CL–CCI–60935 at 3–4; CL–FIA–60937 at 3; CL–Working Group–60947 at 10; CL–IECAssn–60949 at 12–13; and CL–CME–60926 at 13 (expressing that such qualification requirements could have the unintended consequences of (1) harming the ability of market participants to effectively manage their risk by preventing the Exchanges from recognizing an otherwise appropriate exemption from federal speculative position limits, and (2) stifling future innovation in the development of new commodity derivative products created to meet evolving market needs and demands). *See also* CL–FIA–60937 at 9 (citing the following example: ''For example, CME's New York Mercantile Exchange (''NYMEX'') recently listed the LOOP crude oil storage futures contract (LPS) and IFUS recently listed the world cotton futures contract (WCT). Assuming for purposes of illustration that both of these futures contracts were Referenced Contracts, under the Supplemental Proposal neither NYMEX nor IFUS would be permitted to grant non-enumerated hedge, spread, or anticipatory hedge exemptions during the first year of each contract's existence notwithstanding the extensive experience of these exchanges in administering limits on positions in a variety of similar contracts.''), CL–CME–60926 at 14 (arguing that one year of experience in administering position limits in similar contracts within a particular ''asset class'' would be a more reasonable requirement.), CL–FIA–60937 at 9 (expressing the view that ''the CEA precludes the Commission from establishing limits that apply to ''*bona fide* hedge positions,'' and the ''definition of *bona fide* hedging in CEA Section 4a(c)(2) does not include as relevant criteria whether an exchange contract is actively traded or an exchange has one year of prior experience administering limits on positions in that contract.'' Thus, the CEA does not permit the one year prerequisite.)

Commission authorizing exchanges to grant hedge and spread exemptions, and cited concerns with respect to what they believe to be a conflict of interest that could arise between for-profit exchanges and their exemption-seeking customers. The commenters proposed, instead, that the Commission make any final hedge and spread exemption determinations.[1128]

Commission Reproposal

The Commission is reproposing § 150.10(a)(1), as originally proposed with one clarification explained below. In reproposing § 150.10(a)(1), the Commission provides a basic application process for exchanges that elect to process spread exemption applications to federal limits. This process allows exchanges flexibility while also facilitating the Commission's review of exchange granted exemptions. The Commission notes that exchanges have authority to determine whether or not to apply the § 150.10(a)(1) process to spread exemptions from exchange-set limits that are lower than federal limits.

Regarding the comment that the one-year experience and active trading qualification requirements could harm the ability for market participants to effectively manage their risks because the qualification requirements would limit the number of exchanges that could grant exemptions,[1129] the Commission clarifies that the one-year experience and active trading requirement can be met by any referenced contract in the particular commodity.[1130] This feature allows a broader number of exchanges to grant spread exemptions. Furthermore, the Commission notes that an exchange with no active trading and or experience in any referenced contract in the particular commodity may not have their interests aligned with the CEA's policy objectives for position limits, such as those in CEA section 4a(a)(3)(B).[1131]

Finally, the Commission clarifies that an exchange can petition the Commission for a waiver of the one-year experience requirement pursuant to § 140.99 of the Commission's regulations if such exchange believes that their experience and interests are aligned with the Commission's interests with respect to recognizing spread positions.

Regarding comments that the Commission should be the sole authority to make a final hedge or spread exemption determination, or that the Exchange's one-year of experience administering position limits to its actively traded contract and the Commission's de novo review are inadequate, the Commission disagrees. The Commission believes the exchange's one year of experience administering position limits to its actively traded contract,[1132] and the Commission's de novo review of granted exemptions (afterwards) are adequate to guard against or remedy any conflicts of interest. Also, the Commission notes that § 150.10(a)(4)(vi) requires exchanges should take into account whether granting a spread exemption in a physical commodity derivative would, to the maximum extent practicable, ensure sufficient market liquidity for bona fide hedgers, and not unduly reduce the effectiveness of position limits to: Diminish, eliminate, or prevent excessive speculation; deter and prevent market manipulation, squeezes, and corners; and ensure that the price discovery function of the underlying market is not disrupted.[1133]

b. Proposed § 150.10(a)(2)

Proposed Rule

Proposed § 150.10(a)(2) specifies a non-exclusive list of the type of spreads that an exchange might exempt from position limits, including calendar spreads; quality differential spreads; processing spreads (such as energy ''crack'' or soybean ''crush'' spreads); and product or by-product differential spreads. The Commission pointed out that this list was not exhaustive, but reflected common types of spread activity that might enhance liquidity in commodity derivative markets, thereby facilitating the ability of bona-fide hedgers to put on and offset positions in those markets. For example, trading activity in many commodity derivative markets is concentrated in the nearby contract month, but a hedger might need to offset risk in deferred months where derivative trading activity may be less active. A calendar spread trader could provide such liquidity without exposing himself or herself to the price risk inherent in an outright position in a deferred month. Processing spreads can serve a similar function. For example, a soybean processor might seek to hedge his or her processing costs by entering into a ''crush'' spread, *i.e.,* going long soybeans and short soybean meal and oil. A speculator could facilitate the hedger's ability to do such a transaction by entering into a ''reverse crush'' spread (*i.e.,* going short soybeans and long soybean meal and oil). Quality differential spreads, and product or by-product differential spreads, may serve similar liquidity-enhancing functions when spreading a position in an actively traded commodity derivatives market such as CBOT Wheat against a position in another actively traded market, such as MGEX Wheat.

The Commission anticipated that a spread exemption request might include spreads that were ''legged in,'' that is, carried out in two steps, or alternatively were ''combination trades,'' that is, all components of the spread were executed simultaneously.

This proposal, the Commission observed, would not limit the granting of spread exemptions to positions outside the spot month, unlike the existing spread exemption provisions in current § 150.3(a)(3), or in § 150.5(a)(2)(ii) as proposed in the December 2013 Position Limits Proposal. The proposal responded to specific requests of commenters to permit spread exemptions in the spot month. The Commission pointed out

[1128] *See, e.g.,* CL–Public Citizen–60940 at 3; CL–PMAA–NEFI–60952 at 2; CL–RER2–60962 at 1; CL–AFR–60953 at 2; CL–RER1–60961 at 1; CL–PMAA–NEFI–60952 at 2; CL–RER2–60962 at 1; CL–AFR–60953 at 2 and CL–Better Markets–60928 at 1–5.

[1129] As noted above, according to the commenter, the qualification requirements would limit the number of exchanges that could grant exemptions to those that list the relevant referenced contract and manage position limits in that referenced contract based on the exchanges experience and knowledge of the underlying commodity market that referenced contract.

[1130] As noted above, experience manifests in the people carrying out surveillance in a commodity rather than in an institutional structure. An exchange's experience would be provided through the appropriate experience of the surveillance staff regarding the particular commodity. In fact, the Commission has historically reviewed the experience and qualifications of exchange regulatory divisions when considering whether to designate a new exchange as a contract market or to recognize a facility as a SEF; as such exchanges are new, staff experience has clearly been gained at other exchanges.

[1131] CEA section 4a(a)(3)(B) provides that the Commission shall set limits ''to the maximum extent practicable, in its discretion—to diminish, eliminate, or prevent excessive speculation as described under this section; to deter and prevent market manipulation, squeezes, and corners; to ensure sufficient market liquidity for bona fide hedgers; and to ensure that the price discovery function of the underlying market is not disrupted.'' In addition, CEA section 4a(a)(7) authorizes the Commission to exempt any class of transaction from any requirement it may establish with respect to position limits.

[1132] To avoid confusion, the Commission reiterates that experience manifests in the people carrying out surveillance in a commodity rather than in an institutional structure. An exchange's experience would be provided through the appropriate experience of the surveillance staff regarding the particular commodity.

[1133] As noted in the 2016 Supplemental Position Limits Proposal, the guidance is consistent with the statutory policy objectives for position limits on physical commodity derivatives in CEA section 4a(a)(3)(B). *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38464. The Commission interprets the CEA as providing it with the statutory authority to exempt spreads that are consistent with the other policy objectives for position limits, such as those in CEA section 4a(a)(3)(B). *Id.*

that the CME, for example, recommended ''the Commission reaffirm in DCMs the discretion to apply their knowledge of individual commodity markets and their judgement, as to whether allowing intermarket spread exemptions in the spot month for physical-delivery contracts is appropriate.'' [1134]

The Commission proposed to revise the December 2013 Position Limits Proposal in the manner described above because, as it noted in the 2016 Supplemental Position Limits Proposal as well as in the examples above, permitting spread exemptions in the spot month may further one of the four policy objectives set forth in section 4a(a)(3)(b) of the Act: To ensure sufficient market liquidity for bona fide hedgers.[1135] This policy objective, the Commission observed, was incorporated into the proposal in its requirements that: (i) The applicant provide detailed information demonstrating why the spread position should be exempted from position limits, including how the exemption would further the purposes of CEA section 4a(a)(3)(B); [1136] and (ii) the exchange would determine whether the spread position (for which a market participant was seeking an exemption) would further the purposes of CEA section 4a(a)(3)(B).[1137] Moreover, the Commission pointed out that it was retaining the ability to review the exchange rules as well as to review how an exchange enforces those rules.[1138]

The Commission also discussed that it was concerned, among other things, about protecting the price discovery process in the core referenced futures contracts, particularly as those contracts approach expiration. Accordingly, as an alternative, the Commission considered whether to prohibit an exchange from granting spread exemptions that would be applicable during the lesser of the last five days of trading or the time period for the spot month.[1139]

Comments Received

Several commenters expressed the view that exchanges must be allowed to use their experience to determine whether to grant spread exemptions in the spot month—including within the last five days of trading. Commenters expressed the view that allowing exchanges to grant spread exemptions in the spot months/last five days would provide liquidity to the market and help convergence between cash and futures markets.[1140]

Eight commenters expressed the view that the Commission should not impose the five-day rule for spread positions in the expiring spot month contract.[1141] The commenters argued that to impose the five-day rule would adversely affect liquidity in the futures market and impair convergence between cash and futures markets and thus the price discovery function of the futures market. The commenters also expressed the view that the Commission's concerns about trading activity in the final days of an expiring futures contract can best be addressed by existing exchange and Commission surveillance programs and the Commission's ''special call'' authority to request information from market participants.

One commenter expressed the view that the Commission should not apply the five-day rule to certain enumerated bona fide hedging positions under proposed § 150.1(3)–(4), cross-commodity hedges under proposed § 150.1(5), or to non-enumerated bona fide hedge, or spread exemptions. Instead, the Commission should permit the Exchanges to determine the facts and circumstances where a market participant may be permitted to hold a physical-delivery referenced contract in the spot month as part of a position that is exempt from federal speculative position limits.[1142]

Another commenter expressed that it ''would support the applicability of the spread exemption through the end of the month, without limiting the exemption during the current month.'' In that regard, the commenter (an exchange) noted that its ''futures contracts on electricity settle to the independent, spot market overseen by the ISO/RTO markets.'' The commenter argued that ''since the settlement prices are determined in the ISO/RTO markets, trading during the last five days of the spot month has no impact on final settlement prices'' on either the exchange or the ISO/RTO spot markets. The commenter noted that ''bona fide hedgers rely on the ability to hold positions through the end of the current month, which has very low volume traded for monthly power contracts. Restrictions on spread exemptions during the last five days of trading may force market participants to exit their position during a period of lower liquidity—more than 99% of trading volume occurs outside the current (spot) month'' on its exchange.[1143]

One commenter expressed that it is concerned that the new Form 504 would impose a series of reporting requirements to track and distinguish between types of hedge exemptions and requires reporting of all cash market holdings for each day of the spot month that would be difficult given the portfolio nature of commenter's business and the fungibility of futures contracts and the underlying cash commodity. The commenter expressed the view that once a hedge exemption is granted under the supplemental, the reporting requirements should be similar to the reporting requirements for existing enumerated bona fide hedging position exemptions.[1144]

Another commenter expressed the view that it is not necessary to condition spread exemptions on additional filings to the exchange or the Commission.[1145]

Two commenters requested that the Commission clarify that the term ''spread position'' includes all types of spreads and the list of spreads referenced in proposed § 150.10 is simply illustrative and not exhaustive.[1146]

Three commenters requested that the Commission continue to permit cash and carry exemptions, stating, among other reasons, such exemptions serve an economic purpose by helping to maintain an appropriate economic relationship between the nearby and the next successive delivery month.[1147]

Commission Reproposal

The Commission is reproposing § 150.10(a)(2), as originally proposed, and clarifying that the five-day rule does not apply to spreads. Because the Commission did not propose in the 2016 Supplemental Position Limits Proposal to apply the five-day rule to ''spread positions'', exchanges would have discretion to recognize such spread positions without regard to the five-day rule. The Commission cautions exchanges to carefully consider whether

[1134] CL–CME–59718 at 71. *See also* 2016 Supplemental Position Limits Proposal, 81 FR at 38478.

[1135] CEA section 4a(a)(3)(B)(iii); 7 U.S.C. 6a(a)(3)(B)(iii). *See also* the discussion of proposed § 150.10(a)(3)(ii), below.

[1136] *See* proposed § 150.10(a)(3)(ii).

[1137] *See* proposed § 150.10(a)(4)(vi); *see also* 2016 Supplemental Position Limits Proposal, 81 FR at 38478.

[1138] The Commission pointed out that it could, for example, revoke or confirm exchange-granted exemptions.

[1139] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38478.

[1140] CL–ICE–60929 at 24; CL–IECAssn–60949 at 15; and CL–ADM–60934 at 6–7.

[1141] CL–NCGA–ASA–60917 at 1–2; CL–CME–60926 at 3; CL–ICE–60929 at 9; and CL–AFIA–60955 at 2; CL–NGFA–60941 at 5–7; CL–ISDA–60931 at 10; CL–NCFC–60930 at 3–4; and CL–Working Group–60947 at 7–9.

[1142] CL–CCI–60935 at 8–9.

[1143] CL–Nodal–60948 at 3.

[1144] CL–ADM–60934 at 8.

[1145] CL–ICE–60929 at 25.

[1146] CL–Working Group–60947 at 9–10 and CL–FIA–60937 at 14.

[1147] CL–ICE–60929 at 11–12; CL–NCC–ACSA–60972 at 2; and CL–CMC–60950 at 11–12.

to recognize a spread position in the last few days of trading in physical-delivery contracts. For a more detailed discussion please see § 150.9(a)(1) above.

The Commission reiterates, as proposed and discussed in the 2016 Supplemental Position Limit Proposal, that an exchange would not be permitted to recognize a spread between a commodity index contract and one or more referenced contracts. That is, an exchange may not grant a spread exemption where a bona fide hedging position could not be recognized for a pass-through swap offset of a commodity index contract. For a more detailed discussion please see § 150.9(a)(1) above.

In response to the comment regarding spread exemptions for electricity contracts, the Commission notes that electricity contracts are not referenced contracts that will be subject to federal limits at this time. Thus, exchanges may elect to process spread exemptions for exchange-set position limits for non-referenced contracts.

In response to the comments regarding the proposed spread exemption process imposing additional filing requirements on market participants relying on an exchange-granted spread exemption, the Commission clarifies that it is in the exchange's discretion to determine whether there are additional reporting requirements for a spread exemption. For a more detailed discussion please see § 150.9(a)(1) above.

In response to the comments received requesting clarification that the list of spreads in § 150.10(a)(2) [1148] is simply illustrative and not an exhaustive list of possible spread exemptions that may be granted by an exchange, the Commission acknowledges that the list of spreads in § 150.10(a)(2) is not an exhaustive list and that exchanges may grant other spread exemptions so long as they meet the requirements in § 150.10(a)(1), (3), and (4)(vi).

In response to the comments received that requested the Commission continue to permit ''cash and carry'' spread exemptions, the Commission has determined to allow exchanges to grant ''cash and carry'' spread exemptions to exchange and federal limits so long as an exchange has suitable safeguards in place to require a market participant relying on such an exemption to reduce their position below the speculative limit in a timely manner once current market prices no longer permit entry into a full carry transaction. The Commission notes that the condition noted above is more stringent than how ICE Futures U.S. has conditioned market participants relying on a cash-and–carry spread exemption. In that regard, ICE Futures U.S. has required a market participant to reduce their positions ''before the price of the nearby contract month rises to a premium to the second (2nd) contract month.''

c. Proposed § 150.10(a)(3)

Proposed Rule

Proposed § 150.10(a)(3) set forth a core set of information and materials that all applicants would be required to submit to enable an exchange to determine, and the Commission to verify, whether the facts and circumstances attendant to a spread position furthered the policy objectives of CEA section 4a(a)(3)(B). In particular, the applicant would be required to demonstrate, and the exchange to determine, that exempting the spread position from position limits would, to the maximum extent practicable, ensure sufficient market liquidity for bona fide hedgers, but not unduly reduce the effectiveness of position limits to: Diminish, eliminate or prevent excessive speculation; deter and prevent market manipulation, squeezes, and corners; and ensure that the price discovery function of the underlying market is not disrupted.[1149]

The proposal pointed out that one DCM, ICE Futures U.S., currently grants certain types of spread exemptions that the Commission was concerned may not be consistent with these policy objectives.[1150] ICE Futures U.S. allows ''cash-and-carry'' spread exemptions to exchange-set limits, which permit a market participant to hold a long position greater than the speculative limit in the spot month and an equivalent short position in the following month in order to guarantee a return that, at minimum, covers its carrying charges, *such as* the cost of financing, insuring, and storing the physical inventory until the next expiration.[1151] Market participants are able to take physical delivery in the nearby month and redeliver the same product in a deferred month, often at a profit. The Commission noted that while market participants are permitted to re-deliver the physical commodity, they are under no obligation to do so.[1152]

ICE Futures U.S.'s rules condition the cash-and-carry spread exemption upon the applicant's agreement that ''before the price of the nearby contract month rises to a premium to the second (2nd) contract month, it will liquidate all long positions in the nearby contract month.'' [1153] The Commission noted that it understood that ICE Futures U.S. required traders to provide information about their expected cost of carry, which was used by the exchange to determine the levels by which the trader has to reduce the position. Those exit points were then communicated to the applicant when the exchange responded to the trader's spread exemption request.

The 2016 Supplemental Position Limits Proposal considered whether to impose on the exchange a requirement to ensure that exit points in cash-and-carry spread exemptions would facilitate an orderly liquidation in the expiring futures contract. The Commission stated that it was concerned that a large demand for delivery on cash and carry positions might distort the price of the expiring futures upwards. This would particularly be a concern in those commodity markets where the cash spot price was discovered in the expiring futures contract.

As the Commission noted, ICE Futures U.S. opined in a recent rule enforcement review that such exemptions are ''beneficial for the market, particularly when there are plentiful warehouse stocks, which

[1148] Proposed § 150.10(a)(2) included the following list of spreads that a designated contract market or swap execution facility may approve under this section include: (i) Calendar spreads; (ii) Quality differential spreads; (iii) Processing spreads; and (iv) Product or by-product differential spreads.

[1149] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38479, n. 192, and accompanying text (describing the DCM's responsibility under its application process to make this determination in a timely manner).

[1150] *See* ICE Futures U.S. Rule 6.29(e).

[1151] Carrying charges include insurance, storage fees, and financing costs, as well as other costs such as aging discounts that are specific to individual commodities. The ICE Futures U.S. rules require an applicant to provide: (i) Its cost of carry; (ii) the minimum spread at which the applicant will enter into a straddle position and which would result in an profit for the applicant; and (iii) the quantity of stocks in exchange-licensed warehouses that it already owns. The applicant's entire long position carried into the notice period must have been put on as a spread at a differential that covers the applicant's cost of carry. *See* Rule Enforcement Review of ICE Futures U.S., July 22, 2014 (''ICE Futures U.S. Rule Enforcement Review''), at 44–45, available at *http://www.cftc.gov/IndustryOversight/TradingOrganizations/DCMs/dcmruleenf*. *See also* 2016 Supplemental Position Limits Proposal, 81 FR at 38479, n. 189.

[1152] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38479.

[1153] ICE Futures U.S. Rule 6.29(e) (at the time of the target period of the ICE Futures U.S. Rule Enforcement Review (June 15, 2011 to June 15, 2012), the cash-and-carry provision currently found in ICE Futures U.S. Rule 6.29(e) was found in ICE Futures U.S. Rule 6.27(e)). Further, under the exchange's rules, additional conditions may also apply.

typically is the only time when the opportunity exists to utilize the exemption,'' maintaining that the exchange's rules and procedures are effective in ensuring orderly liquidations.[1154] The Commission observed that it remained concerned about these exemptions and their impact on the spot month price, and noted that it was still reviewing the effectiveness of the exchange's cash-and-carry spread exemptions and the procedure by which they were granted.

As an alternative to providing exchanges with discretion to consider granting cash-and-carry spread exemptions, the Commission considered, in the 2016 Supplemental Position Limits Proposal, prohibiting cash-and-carry spread exemptions to position limits. In this regard, the Commission pointed out that it does not grant such exemptions to current federal position limits. As another alternative, the Commission considered permitting exchanges to grant cash-and-carry spread exemptions, but would require suitable safeguards be placed on such exemptions. For example, the Commission considered requiring that cash-and-carry spread exemptions be conditioned on a market participant reducing positions below speculative limit levels in a timely manner once current market prices no longer permit entry into a full carry transaction, rather than the less stringent condition of ICE Futures U.S. that a trader reduce positions ''before the price of the nearby contract month rises to a premium to the second (2nd) contract month.'' [1155]

Comments Received

One commenter expressed the view that an ''exchange should not be required to determine whether liquidity will be increased if a particular Spread Exemption is granted before it is permitted to grant such Spread Exemption.'' According to the commenter, ''this requirement effectively would create an entirely new legal standard for spread exemptions and flip on its head the requirement under CEA section 4a(a)(3)(b)(iii), which states that, to the maximum extent practicable, in establishing speculative position limits the Commission in its discretion should ensure sufficient market liquidity for bona fide hedgers. CEA section 4a(a)(3)(b)(iii) does not require (and should not require) that, in granting an exemption from speculative position limits, the exemption must add to liquidity.'' [1156]

Two commenters requested that the proposed application requirements for market participants be revised to only require ''such information as the relevant exchange deems necessary to determine if the requested exemption is consistent with the purposes of hedging.'' Furthermore one commenter requested that the Commission confirm that the detailed procedures for exchange-granted exemptions for spread and anticipatory hedges are not applicable to exemptions granted by exchanges for positions below the federal level.[1157]

One commenter expressed the view that ''if proposed Regulations 150.9(a)(3)(iii) and 150.10(a)(3)(iii) indeed are intended to apply to an applicant's maximum size of all gross positions for each and every commodity derivative contract the applicant holds (as opposed to the maximum gross positions in the commodity derivative contract(s) for which the exemption is sought), such requirements are unnecessary and unduly burdensome.'' [1158]

Commission Reproposal

The Commission is reproposing § 150.10(a)(3), largely as originally proposed with one clarifying amendment to § 150.10(a)(3)(iii), as discussed further below. The Commission believes that exchanges should consider the policy objectives of CEA section 4a(a)(3)(B), which is the standard that the Commission would use to review a petition to exempt a spread position from position limits. Regarding the comment arguing that CEA section 4a(a)(3)(b)(iii) does not require that the granting of a spread exemption must increase liquidity, the Commission interprets the CEA as providing it with the statutory authority to exempt spreads that are consistent with the other policy objectives for position limits, such as those in CEA section 4a(a)(3)(B). CEA section 4a(a)(3)(B) provides that the Commission shall set limits to the maximum extent practicable, in its discretion—to diminish, eliminate, or prevent excessive speculation as described under this section; to deter and prevent market manipulation, squeezes, and corners; to ensure sufficient market liquidity for bona fide hedgers; and to ensure that the price discovery function of the underlying market is not disrupted. The Commission believes that exchanges who elect to grant spread exemptions to federal position limits should use the guidance in CEA section 4a(a)(3)(B) as the Commission would when reviewing de novo a spread exemption application.

Regarding the comment requesting change to the requirements of § 150.10(a)(3) to only require ''such information as the relevant exchange deems necessary to determine if the requested exemption is consistent with the purposes of hedging,'' the Commission believes that the proposal requires a minimum amount of information, and exchanges have discretion to require additional information. If (as one commenter represented) an exchange has market information that would supplement its analysis of a spread exemption application, nothing in the proposal would preclude an exchange from using that information in its analysis. However, the Commission notes that such information must be included in the records of that spread exemption application as required under § 150.10(b).

In response to the request for clarification regarding whether § 150.10 applies to both federal and exchange-set limits, the Commission clarifies that, as

[1154] ICE Futures U.S. Rule Enforcement Review, at 45.

[1155] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38479.

[1156] CL–Working Group–60947 at 22. *See also* CL–ISDA–60931 at 1 (expressing that under the 2016 Supplemental Position Limits Proposal, the exchange must certify that a spread exemption increases liquidity in order to grant it. The commenter expressed the view that the CEA requires limits that do not impair liquidity, as opposed to limits that specifically increase it. Furthermore, the commenter recommended that the Commission should remove this condition because the purpose of a spread exemption ''is not to increase liquidity but rather to recognize the more limited speculative opportunity created by such positions.'').

[1157] CL–ICE–60929 at 8. *See also* CL–Nodal–60948 at 2–3 (expressing the view that ''[t]he Proposed Rule is overly prescriptive as to the information that must be provided by the applicant, especially when the exchange may have superior information regarding intramarket spreads. Unlike intermarket spreads, the exchange, and not the applicant, is more likely to have direct information to determine whether an intramarket spread achieves the goals of CEA 4a(a)(3)(B). For example, [an exchange] has current deliverable supply analysis, spread and outright trading activity information, and market data from spot markets for the underlying physical commodities. In performing its pricing and surveillance functions, [an exchange] monitors position accumulation information that is not available to market participants as well as out-of-market pricing in real time.'' The commenter requested that it be allowed to determine its application process, and the information it needs to achieve the policy objectives of CEA 4a(a)(3)(B), ''for which the Commission has the authority to review the exchange's rules and conclusions.'')

[1158] CL–Working Group–60947 at 10. *See also* CL–ISDA–60931 at 10 (expressing the view that the proposed rule 150.10(a)(3)(iii) requiring maximum size of all gross positions in derivative contracts is too broad and practically impossible as no market participant can predict trading activity for a year).

explained above in connection with § 150.5, § 150.10 would not apply if an exchange grants exemptions from speculative position limits it sets under paragraph § 150.5(a)(1), provided that that any spread exemptions to exchange-set limits not conforming to § 150.3 and § 150.10 were capped at the level of the applicable federal limit in § 150.2. Further, § 150.10 would not apply to exchanges that grant spread exemptions to exchange-set limits, in commodity derivative contracts not subject to a federal limit.

Regarding the comment about whether the phrase ''maximum size of all gross positions'' applies to an applicant's entire book of derivative positions or just those positions pertaining to the exemption application, the Commission intended that the applicant only report its maximum size of all gross positions in the commodity related to the exemption application that it is submitting. In that regard, Commission is reproposing § 150.10(a)(3)(iii) to clarify as such. For a more detailed discussion, please see § 150.9(a)(2) above.

d. Proposed § 150.10(a)(4)

Proposed Rule

Proposed § 150.10(a)(4) set forth certain timing requirements that an exchange would be required to include in its rules for the spread application process. Those timing requirements would substantially mirror those provisions proposed in § 150.9(a)(4) [1159] for the non-enumerated bona fide hedging position application process. While these timing requirements are similar to those under proposed § 150.9(a)(4), the exchange, under proposed § 150.10(a)(4), must also determine in a timely manner whether the facts and circumstances attendant to a position further the policy objectives of CEA section 4a(a)(3)(B).[1160]

Comments Received

The Commission notes that it did not receive comments regarding § 150.10(a)(4).

Commission Determination

The Commission is reproposing § 150.10(a)(4), as originally proposed.

e. Proposed § 150.10(a)(5)

Proposed Rule

Proposed § 150.10(a)(5) clarified that an applicant's spread position would be deemed to be recognized as a spread position exempt from federal position limits at the time an exchange recognized it. The Commission noted that this was substantially similar to proposed § 150.9(a)(5) for non-enumerated bona fide hedging position exemptions.[1161]

Comments Received

One commenter expressed the view that it is concerned regarding how an exchange should coordinate the granting of exemptions with respect to contracts on the same underlying commodities that trade on different exchanges, and requests guidance from the Commission on that matter.[1162]

Commission Reproposal

The Commission is reproposing § 150.10(a)(5), as originally proposed. The Commission notes that the proposal allows each exchange to use its own expertise to decide what exemptions and limit levels to employ for their venue with the Commission serving in an oversight role to monitor exemptions and position limits across exchanges. The Commission also notes that although the proposal does not address coordination of granting of exemptions among exchanges, there is nothing in the proposal that would prohibit exchanges from coordinating.

f. Proposed § 150.10(a)(6)

Proposed Rule

Proposed § 150.10(a)(6) required exchanges that elect to process spread applications to promulgate reporting rules for applicants who owned, held or controlled positions recognized as spreads; the Commission noted that this is substantially similar to proposed § 150.9(a)(6) for non-enumerated bona fide hedge exemptions.[1163]

Comments Received

Several commenters [1164] recommended, ''that the Commission remove the proposed requirement that an exchange must adopt enhanced reporting rules for market participants that rely on non-enumerated hedge exemptions, spread exemptions, or anticipatory exemptions'' because the proposal ''would force exchanges to establish rules that require market participants to report all referenced contract positions that they hold or control in reliance upon a non-enumerated hedge, spread, or anticipatory hedge exemption along with the underlying cash market exposure (*e.g.,* cash positions or components of a spread) hedged by those positions.'' Many of these commenters expressed the view that such reporting requirements would be overly burdensome and/or confusing.

Commission Reproposal

The Commission is reproposing § 150.10(a)(6) with one modification to clarify in the regulation text that exchanges are authorized, but not required, to determine whether to require reporting by the spread exemption applicant. For a more detailed discussion, please see the discussion of § 150.9(a)(3) above.

g. Proposed § 150.10(a)(7)

Proposed Rule

Proposed § 150.10(a)(7) required an exchange to publish on its Web site, no less frequently than quarterly, a description of each new type of derivative position that it recognized as a spread; the Commission noted that this was substantially similar to proposed § 150.9(a)(7) for non-enumerated bona fide hedging position exemptions.[1165]

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[1159] The Commission noted, for example, proposed § 150.9(a)(4) provided that: (i) A person intending to rely on a exchange's exemption from position limits would be required to submit an application in advance and to reapply at least on an annual basis; (ii) the exchange would be required to notify an applicant in a timely manner whether the position was exempted, and reasons for any rejection; and (iii) the exchange would be able to revoke, at any time, any recognition previously issued pursuant to proposed § 150.9 if the exchange determined the recognition was no longer in accord with section 4a(c) of the Act. *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38480, n. 192.

[1160] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38476, n. 171 and accompanying text.

[1161] For example, proposed § 150.9(a)(5) provided that the position will be deemed to be recognized as a non-enumerated bona fide hedging position when an exchange recognized it.

[1162] CL–ISDA–60931 at 6–7.

[1163] For example, proposed § 150.9(a)(6) provided that an exchange would promulgate enhanced reporting rules in order to obtain sufficient information to conduct an adequate surveillance program to detect and potentially deter excessively large positions that might disrupt the price discovery process.

[1164] *See, e.g.,* CL–FIA–60937 at 15; CL–CMC–60950 at 12–13; CL–CCI–60935 at 7–8; CL–NCGA–NGSA–60919 at 12–13; CL–MGEX–60936 at 6; CL–ISDA–60931 at 10; CL–NGFA–60941 at 4; CL–Working Group–60947 at 12 (footnotes omitted) and CL–AMG–60946 at 4–5.

[1165] For example, proposed § 150.9(a)(7) provided that an exchange would publish on its Web site, no less frequently than quarterly, a description of each new type of derivative position that it recognized as a non-enumerated bona fide hedge. The Commission noted that it envisioned that each description would be an executive summary. The description would be required to include a summary describing the type of derivative position and an explanation of why it qualified as a non-enumerated bona fide hedge. The Commission observed that the exchanges were in the best position when quickly crafting these descriptions to accommodate an applicant's desire for trading

Continued

Comments Received

One commenter expressed the view that proposed § 150.10 would have an anti-competitive effect on markets that rely on intramarket spread trading to enhance liquidity on less actively traded contracts. The commenter was concerned that the information that would be published in a fact pattern summary would provide details that could be used to identify market participants, especially in thinly traded specialized markets.[1166]

Another commenter expressed the view that exchanges should ''not be required to disclose any conditions of an exemption granted due to the potential for such information to compromise the exemption recipient's position.'' [1167]

Commission Reproposal

The Commission is reproposing § 150.10(a)(6), as originally proposed. The Commission reiterates that the purpose of each summary is to provide transparency to market participants by providing fair and open access for market participants to information regarding which positions might be recognized as spreads. The summary would be an executive summary that does not provide details of a market participant who received such an exemption, but rather, a general description of what the position is and why it qualifies for a spread exemption. The commenters did not provide any proposed alternatives to provide such transparency to market participants.

h. Proposed § 150.10(a)(8)

Proposed Rule

Proposed § 150.10(a)(8) provided options for an exchange to elect to request the Commission review a spread application that raised novel or complex issues, using the process set forth in proposed § 150.10(d), discussed below.[1168] This was substantially similar to those proposed under § 150.9(a)(8).[1169]

Comments Received

The Commission did not receive comments regarding § 150.10(a)(8).

Commission Reproposal

The Commission is reproposing § 150.10(a)(8), as originally proposed.

i. Proposed § 150.10(b)—Recordkeeping Requirements

Proposed Rule

Proposed § 150.10(b) outlined the recordkeeping requirements for exchanges that elected to process spread exemption applications submitted pursuant to § 150.10(a). As noted above, the proposed processes under this rule were substantially similar to the corresponding provisions in § 150.9(b). Hence, the Commission does not repeat the discussion here.

Commission Reproposal

The Commission did not receive comments on § 150.10(b), and is reproposing this rule, as originally proposed, for the same reasons as discussed in connection with § 150.9(b).

j. Proposed § 150.10(c) (Exchange Reporting) and Reproposal

Proposed Rule

Proposed § 150.10(c)(1) required designated contract markets and swap execution facilities that elected to process spread exemption applications to submit to the Commission a report for each week as of the close of business on Friday showing various information concerning the derivative positions that had been recognized by the designated contract market or swap execution facility as an exempt spread position, and for any revocation, modification or rejection of such recognition. Moreover, proposed § 150.10(c)(2) required a designated contract market or swap execution facility that elected to process applications for exempt spread positions to submit to the Commission (i) a summary of any exempt spread position newly published on the designated contract market or swap execution facility's Web site; and (ii) no less frequently than monthly, any report submitted by an applicant to such designated contract market or swap execution facility pursuant to rules required under proposed § 150.10(a)(6).[1170]

As noted above, the proposed processes under this rule were substantially similar to the corresponding provisions in § 150.9(c). The Commission did not receive comments on this section that differed from those received on § 150.9(c).

Commission Reproposal

The Commission is reproposing this rule, largely as originally proposed, for the reasons previously provided in the discussion regarding § 150.9(c), with the same revision to the regulatory text included in reproposed § 150.9(c), to clarify that exchanges have the discretion to determine whether to incorporate additional reporting requirements for spread exemption applicants. In particular, the Commission is proposing to amend language in § 150.10(c)(2) to clarify that, unless otherwise instructed by the Commission, an exchange that elects to process applications to exempt spread positions from position limits shall submit to the Commission, no less frequently than monthly, ''any reports such [DCM or SEF] requires to be submitted by an applicant to such [DCM or SEF] pursuant to the rules required under paragraph (a)(6) of this section.''

k. Proposed § 150.10(d) (Review of applications by the Commission) and Reproposal

Proposed Rule

Proposed § 150.10(d) provided for Commission review of applications to ensure that the processes administered by the exchange, as well as the results of such processes, were consistent with the purposes of section 4a(a)(3)(B) of the Act and the Commission's regulations thereunder. As noted previously, under the proposal, the Commission was not diluting its ability to grant or not grant spread exemptions. The Commission reserved to itself the ability to review any exchange action, and to review any application by a market participant to an exchange, whether prior to or after disposition of such application by an exchange. An exchange could ask the Commission to consider a spread exemption application (proposed § 150.10(a)(8)). The Commission could also on its own initiative at any time—before or after action by an exchange—review any application submitted to an exchange for recognition of a spread exemption (proposed § 150.10(d)(1)). And, as noted above, market

anonymity while promoting fair and open access for market participants to information regarding which positions might be recognized as non-enumerated bona fide hedges.

[1166] CL–Nodal–60948 at 4.

[1167] CL–CME–60926 at 11.

[1168] If the exchange determined to request under proposed § 150.10(a)(8) that the Commission consider the application, the exchange must, under proposed § 150.10(a)(4)(v)(C), notify an applicant in a timely manner that the exchange had requested that the Commission review the application. This provision provided the exchanges with the ability to request Commission review early in the review process, rather than requiring the exchanges to process the request, make a determination and only then begin the process of Commission review provided for under proposed § 150.10(d). The Commission noted that although most of its reviews would occur after the exchange makes its determination, the Commission could, as provided for in proposed § 150.10(d)(1), initiate its review, in its discretion, at any time.

[1169] For example, proposed § 150.9(a)(8) provided that if an exchange makes a request pursuant to proposed § 150.9(a)(8), the Commission, as would be the case for an exchange, would not be bound by a time limitation.

[1170] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38480; *see also* discussion of 150.9(c) at 38474–75.

participants would still be able to request a staff interpretive letter under § 140.99 from the Commission or seek exemptive relief under CEA section 4a(a)(7) from the Commission, as an alternative to the three proposed exchange-administered processes.

As previously indicated, the processes under the proposed rule was substantially similar to the corresponding provisions in proposed § 150.9(d). Hence, the Commission does not repeat the discussion here.

Commission Reproposal

The Commission did not receive comments on this section that differed from those received on § 150.9(d), and is reproposing this rule, as originally proposed, for the reasons discussed above in connection with § 150.9(d).

l. Proposed § 150.10(e) (Review of summaries by the Commission) and Reproposal

Proposed Rule

The Commission proposed to rely on the expertise of the exchanges to summarize and post executive summaries of spread exemptions to their respective Web sites under proposed § 150.10(a)(7). The Commission also proposed, in § 150.10(e), to review such executive summaries to ensure they provided adequate disclosure to market participants of the potential availability of relief from speculative position limits.

Commission Reproposal

As noted above, the proposed processes under this rule are substantially similar to the corresponding provisions in § 150.9(e). The Commission did not receive comments on this section that differed from those received on § 150.9(e), and so does not repeat the discussion here. For all the reasons previously provided, the Commission is reproposing this rule, as originally proposed.

m. Proposed § 150.10(f) (Delegation of Authority) and Reproposal

Proposed Rule

The Commission proposed to delegate certain of its authorities under proposed § 150.10 to the Director of the Commission's Division of Market Oversight, or such other employee or employees as the Director designated from time to time. Proposed § 150.10(f)(1)(i) delegated the Commission's authority to the Division of Market Oversight to provide instructions regarding the submission of information required to be reported to the Commission by an exchange, and to specify the manner and determine the format, coding structure, and electronic data transmission procedures for submitting such information. Proposed § 150.10(f)(1)(v) delegated the Commission's review authority under proposed § 150.10(e) to DMO with respect to summaries of the types of spread exemptions that were required to be posted on an exchange's Web site pursuant to proposed § 150.10(a)(7).

Proposed § 150.10(f)(1)(i) delegated the Commission's authority to the Division of Market Oversight to agree to or reject a request by an exchange to consider an application for recognition of an application for a spread exemption. Proposed § 150.10(f)(1)(iii) delegated the Commission's authority to review any application for a spread exemption, and all records required to be maintained by an exchange in connection with such application. Proposed § 150.10(f)(1)(iii) also delegated the Commission's authority to request such records, and to request additional information in connection with such application from the exchange or from the applicant.

Proposed § 150.10(f)(1)(iv) delegated the Commission's authority, under proposed § 150.10(d)(2) to determine when an application for a spread exemption required additional analysis or review, and to provide notice to the exchange and the particular applicant that they had 10 days to supplement such application.

The Commission did not propose to delegate its authority under proposed § 150.10(d)(3) to make a final determination as to the exchange's disposition. The Commission stated that if an exchange's disposition raised concerns regarding consistency with the Act or presents novel or complex issues, then the Commission should make the final determination, after taking into consideration any supplemental information provided by the exchange or the applicant.[1171]

Commission Reproposal

As noted above, the proposed processes under this rule are substantially similar to the corresponding provisions in § 150.9(f); the Commission did not receive comments on this section that differed from those received on § 150.9(f), and so does not repeat the discussion here. For all the reasons previously provided, the Commission is reproposing § 150.9(f), as originally proposed.

[1171] *See* 2016 Supplemental Position Limits Proposal, 81 FR 38482, Jun. 13, 2016.

*I. § 150.11—Process for Recognition of Positions As Bona Fide Hedging Positions for Unfilled Anticipated Requirements, Unsold Anticipated Production, Anticipated Royalties, Anticipated Services Contract Payments or Receipts, or Anticipatory Cross-Commodity Hedge Positions*

1. Overview of the Enumerated Anticipatory Bona Fide Hedging Position Exemption Proposal

After reviewing comments in response to the December 2013 Position Limits Proposal, the Commission proposed another method by which market participants may have enumerated anticipatory bona fide hedge positions recognized. As proposed in the December 2013 Position Limits Proposal, § 150.7 would require market participants to file statements with the Commission regarding certain anticipatory hedges which would become effective absent Commission action or inquiry ten days after submission. As the Commission explained in the 2016 Supplemental Position Limits Proposal, the method in proposed § 150.11 was an exchange-administered process to determine whether certain enumerated anticipatory bona fide hedge positions, such as unfilled anticipated requirements, unsold anticipated production, anticipated royalties, anticipated service contract payments or receipts, or anticipatory cross-commodity hedges should be recognized as bona fide hedge positions.[1172]

The Commission noted that proposed § 150.11 worked in concert with the following three proposed rules:

- Proposed § 150.3(a)(1)(i), with the effect that recognized anticipatory enumerated bona fide hedging positions may exceed federal position limits;
- proposed § 150.5(a)(2), with the effect that recognized anticipatory enumerated bona fide hedging positions may exceed exchange-set position limits for contracts subject to federal position limits; and
- proposed § 150.5(b)(5), with the effect that recognized anticipatory enumerated bona fide hedging positions may exceed exchange-set position limits for contracts not subject to federal position limits.[1173]

The proposed § 150.11 process was somewhat analogous to the application process for recognition of non-enumerated bona fide hedging positions under proposed § 150.9. The process for recognition of enumerated anticipatory

[1172] *Id.* at 38495.

[1173] *Id.*

bona fide hedging positions contained five paragraphs: (a) through (e). The first three paragraphs—§ 150.11(a), (b), and (c)—required exchanges that elected to have a process for recognizing enumerated anticipatory bona fide hedging positions, and market participants that sought position-limit relief for such positions, to carry out certain duties and obligations. The fourth and fifth paragraphs—§ 150.11(d), and (e)—delineated the Commission's role and obligations in reviewing requests for recognition of enumerated anticipatory bona fide hedging positions.[1174]

The Commission noted that there would be significant benefits related to the adoption of proposed § 150.11. Similar to the benefits for recognizing positions as non-enumerated bona fide hedging positions under § 150.9, recognizing anticipatory positions as bona fide hedging posiitons under § 150.11 would provide market participants with potentially a more expeditious recognition process than the Commission proposal for a 10-day Commission recognition process under proposed § 150.7. This could potentially enable commercial market participants to pursue trading strategies in a more timely fashion to advance their commercial and hedging needs to reduce risk. In addition, the Commission pointed out that exchanges would be able to use existing resources and knowledge in the administration and assessment of enumerated anticipatory bona fide hedging positions. The Commission and exchanges have evaluated these types of positions for years (as discussed in the December 2013 Position Limits Proposal).[1175]

The Commission also pointed out that proposed § 150.11, similar to proposed § 150.9 and § 150.10, also would provide the benefit of enhanced record-retention and reporting of positions recognized as enumerated anticipatory bona fide hedging positions. As previously discussed, records retained for specified periods would enable exchanges to develop consistent practices and afford the Commission accessible information for review, surveillance, and enforcement efforts. Likewise, weekly reporting under § 150.11 would facilitate the Commission's tracking of such exemptions.[1176]

2. Proposed § 150.11(a)

Proposed Rule

As noted, proposed § 150.11(a) permitted exchanges to recognize certain enumerated anticipatory bona fide hedging positions, such as unfilled anticipated requirements, unsold anticipated production, anticipated royalties, anticipated service contract payments or receipts, or anticipatory cross-commodity hedges. The proposed rule allowed market participants to work with exchanges to seek the exemption.

The process under proposed § 150.11(a) was similar to the process under proposed § 150.9(a), described above. For example, an exchange with at least one year of experience and expertise administering position limits could elect to adopt rules to recognize commodity derivative positions as enumerated anticipatory bona fide hedges. However, the § 150.11(a) process was different from the process under proposed § 150.9(a) in that the Commission did not propose to permit separate processes for applications based on novel versus non-novel facts and circumstances.[1177]

As the Commission noted in the 2016 Supplemental Position Limits Proposal, it determined to define certain anticipatory positions as enumerated bona fide hedging positions when it adopted current § 1.3(z)(2); the Commission did not change this determination in the December 2013 Position Limits Proposal.[1178] Consequently, the Commission did not anticipate that applications for recognition of enumerated anticipatory bona fide hedging positions would be based on novel facts and circumstances. For the same reason, proposed § 150.11(a) did not require exchanges to post summaries of any enumerated anticipatory bona fide hedging positions. As the Commission noted, other simplifications follow from this difference.[1179]

Comments Received

Several commenters recommended that the Commission specifically recognize the full scope of anticipatory hedging activities such as anticipatory merchandising and anticipatory processing hedges, utility sales and cross-commodity hedges as enumerated bona fide hedging position exemptions.[1180]

In addition, several commenters recommended that the Commission not adopt the ''active trading'' and ''one year experience'' requirements as proposed regarding a DCM's qualification to administer exemptions from federal position limits.[1181] These commenters stated that such qualification requirements could have the unintended consequences of: (i) harming the ability of market participants to effectively manage their risk by preventing the exchanges from recognizing an otherwise appropriate exemption from federal speculative position limits; and (ii) stifling future innovation in the development of new commodity derivative products created to meet evolving market needs and demands.

Certain commenters opposed the Commission delegating hedge exemption authority to exchanges entirely.[1182] These commenters believed that such delegated authority creates an inherent conflict of interest for exchanges because they are incentivized to increase trading volume. Among other concerns, these commenters fear that hedge exemption applicants may develop a preference for those exchanges more willing to grant exemptions. Further, the exchanges may not have a full picture of the entire market in which they are being asked to grant the exemption.

According to other commenters, the Commission should eliminate the five-day rule.[1183] Instead, these commenters stated, the Commission should specifically authorize exchanges to grant bona fide hedging position exemptions during the last five days of trading or less and allow exchanges to permit commercial hedging into the spot period where the facts and circumstances warrant.

Lastly, several commenters advocated for removal of the proposed requirement that exchanges adopt enhanced reporting requirements for market participants that rely on exchange-administered hedge exemptions.[1184] One argued that such a requirement is not authorized by the CEA and would have the unintended effect of preventing

[1174] *Id.*

[1175] *Id.* at 38496.

[1176] *Id.*

[1177] *Id.* at 38481.

[1178] *Id.*

[1179] *Id.*

[1180] CL- NCC–ACSA–60972 at 2; CL–AGA–60943 at 3; CL–ICE–60929 at 12; CL–CMC–60950 at 6–9; CL–FIA–60937 at 5, 21; CL–API–60939 at 3; and CL–EEI–EPSA–60925 at 13.

[1181] CL–CCI–60935 at 3–4; CL–FIA–60937 at 3; CL–Working Group-60947 at 10; CL–IECAssn–60949 at 12–13 and CL–CME–60926 at 13.

[1182] CL–Public Citizen–60940 at 1–2; CL–RER1–60961 at 1; and CL–Better Markets–60928 at 3–5.

[1183] CL–IECAssn–60949 at 7–9; CL–NCGA–NGSA–60919 at 7; CL–ICE–60929 at 9; CL–CMC–60950 at 9–11; CL–API–60939 at 3; CL–NCC–ACSA–60972 at 2; and CL-Working Group–60947 at 7.

[1184] CL–FIA–60937 at 3; and CL–CMC–60950 at 12–13.

new entrants to the relevant market.[1185] Another further argues that these enhanced reporting requirements are unnecessary, impose undue cost burdens on commercial end-users, and the Commission can always request the information through its existing authority.[1186] And two suggest that the Commission allow exchanges flexibility to request satisfactory data, but not set a fixed prerequisite time period to obtaining exemptions.[1187]

Commission Reproposal

After carefully considering the comments received, the Commission is reproposing the rule, as originally proposed. At this time the Commission has already proposed several enumerated bona fide hedging position exemption categories. At this time, the Commission believes that additional fact patterns for bona fide hedging position exemptions will require consideration of the facts and circumstances on a case-by-case basis. The Commission is willing to explore further additions to the enumerated list at a later date. However, the Commission reiterates that, as previously discussed, an exchange can petition under § 13.2 for Commission recognition of a generic fact pattern as an enumerated bona fide hedging position, and that market participants have the flexibility of two processes for recognition of a position as an enumerated bona fide hedging position: (i) request an exemptive, no-action or interpretative letter under § 140.99; and/or (ii) petition under § 13.2 for changes to Appendix B to part 150.

Separately, as noted in the June 2016 Supplemental Position Limits Proposal and above, the Commission is not persuaded that an exchange with no active trading and no previous experience with a new product class would have their interests aligned with the Commission's policy objectives in CEA section 4a. In addition, as noted above, the Commission points out that the experience is manifested by the people carrying out surveillance rather than tied to a particular exchange.[1188] Further, the Commission believes that the active trading requirement can be satisfied by maintaining any referenced contract listed in the particular commodity at issue. For example, a DCM may immediately begin accepting hedge exemption requests for a new commodity contract pursuant to § 150.11(a) if the DCM already maintains contract(s) in the same underlying commodity class that satisfy the experience and active trading requirements.

The Commission clarifies, however, that an exchange can petition the Commission, pursuant to § 140.99, for a waiver of the one-year experience requirement if such exchange believes that their experience and interested are aligned with the Commission's interests with respect to recognizing enumerated anticipatory bona fide hedging positions.

The Commission appreciates commenter concerns regarding those opposed to delegating any hedge exemption authority to exchanges. However, the Commission reiterates that it retains full oversight authority over exchanges issuing hedge exemptions. Further, the Commission believes an exchange's required experience administering position limits for its actively traded contracts, and the Commission's de novo review of granted hedge exemptions are adequate to guard against or remedy any conflicts of interest that may arise. The Commission also notes that exchanges remain bound by the Commission's bona fide hedging position definition for all hedge exemption determinations conducted pursuant to part 150 of Commission Regulations.

The Commission believes the five-day rule should be applied to anticipatory bona fide hedging positions. If a market participant wishes to secure an exemption from the five-day rule, the participant should submit an exemption request, pursuant to § 150.9, for recognition of a non-enumerated bona fide hedging position.

Further, the Commission believes that reporting requirements applicable to market participants seeking an exemption pursuant to § 150.11 may remain as proposed. The Commission notes that § 150.11(a)(5) clarifies that applicants are bound by the reporting requirements found in § 150.7(e). As noted in § 150.7, understanding the recent history of a firm's production data is necessary to ensure the requested anticipated hedge exemption is reasonable. However, as discussed above, the Commission notes that it may permit a reasonable, supported estimate of, for example, anticipated production for less than three years of annual production data, in the Commission's discretion, if a market participant does not have three years of data. Further, the Commission is amending the applicable form instructions to clarify that Commission staff could determine that such an estimate is reasonable and would be accepted. The Commission is also proposing that exchange staff, on behalf of the Commission, also could permit a reasonable, supported estimate of, for example, anticipated production for less than three years of annual production data.

3. Proposed § 150.11(b) (Recordkeeping) and Reproposal

Proposed Rule

Proposed § 150.11(b) required electing designated contract markets and swap execution facilities to keep full, complete, and systematic records of all activities relating to the processing and disposition of enumerated anticipatory bona fide hedging exemption requests submitted pursuant to § 150.11(a). As previously stated, the Commission believes such recordkeeping requirements are essential to ensure adequate compliance and oversight.

Commission Reproposal

As noted, the proposed processes under this rule are substantially similar to the corresponding provisions in § 150.9(b) and § 150.10(b). Hence, the Commission does not repeat the discussion here. The Commission did not receive comments on § 150.11(b), and is reproposing this rule, as originally proposed, for the same reasons as § 150.9(b) and § 150.10(b).

4. Proposed § 150.11(c) (Exchange Reporting) and Reproposal

Proposed Rule

Proposed § 150.11(c) required designated contract markets and swap execution facilities that elected to process enumerated anticipatory bona fide hedging position applications to submit to the Commission a report for each week as of the close of business on Friday showing various information concerning the derivative positions that had been recognized by the designated contract market or swap execution facility as an enumerated anticipatory bona fide hedging position, and for any revocation, modification or rejection of such recognition. Similar to non-enumerated bona fide hedging positions

[1185] CL–FIA–60937 at 3.

[1186] CL–CMC–60950 at 12–13.

[1187] CL–AMG–60946 at 3–4; and CL–FIA–60937 at 3, 12.

[1188] As the Commission noted above when discussing the requirement for one year of experience in connection with § 150.9(a), experience manifests in the people carrying out surveillance in a commodity rather than in an institutional structure. An exchange's experience could be demonstrated through the relevant experience of the surveillance staff regarding the particular commodity. In fact, the Commission has historically reviewed the experience and qualifications of exchange regulatory divisions when considering whether to designate a new exchange as a contract market or to recognize a facility as a SEF; as such exchanges are new, staff experience has clearly been gained at other exchanges.

and spreads, this rule implemented a weekly reporting obligation for exchanges. Unlike the other hedge exemption application types, exchanges would have no monthly reporting or web-posting obligations related to accepting or granting enumerated anticipatory bona fide hedging position exemptions.

Commission Reproposal

In consideration of these reduced reporting requirements and the previous discussion of this subject regarding proposed §§ 150.9(c) and 150.10(c), the Commission is reproposing this rule, as originally proposed, for the reasons discussed therein.

5. Proposed § 150.11(d) (Review of applications by the Commission) and Reproposal

Proposed Rule

As set forth in proposed § 150.11(d), an exchange could ask the Commission to consider an enumerated anticipatory bona fide hedging position application directly. Further, the Commission could also, on its own initiative, at any time—before or after action by an exchange—review any application submitted to an exchange for recognition of an enumerated anticipatory bona fide hedging position. As noted, alternatives also remain available. Market participants would retain the ability to apply directly to the Commission under § 150.7, to separately request staff interpretive letters pursuant to § 140.99 or seek exemptive relief under CEA section 4a(a)(7).

The review process set forth in § 150.11(d) was simpler than other hedge exemption requests because such applications are not anticipated to be based on novel facts and circumstances. Rather, Commission review would focus on whether the hedge exemption application satisfied the filing requirements contained in § 150.11(a). If the filing was not complete, then proposed § 150.11(d) would provide an opportunity to supplement to the applicant and the exchange.

Commission Reproposal

Aside from this minor difference, the proposed processes under this rule were substantially similar to the corresponding provisions in § 150.9(d) and § 150.10(d). Hence, the Commission does not repeat the discussion here. The Commission believes the proposed *de novo* review of exchange-granted anticipatory bona fide hedging position exemptions is adequate to maintain proper exchange oversight. For all the reasons previously provided above in the discussion regarding § 150.9(d), the Commission is reproposing this rule, as originally proposed.

6. Proposed § 150.11(e) (Delegation of Authority) and Reproposal

Proposed Rule

As noted previously, the Commission proposed to delegate certain of its authorities under § 150.11 to the Director of DMO, or such other employee or employees as the Director may designate from time to time. In particular, proposed § 150.11(e)(1)(ii) delegated the Commission's authority to DMO to provide instructions regarding the submission of information required by an exchange, and to specify the manner and determine the format, coding structure, and electronic data transmission procedures for submitting such information. Proposed § 150.11(e)(1)(i) delegated the Commission's authority to DMO to agree to or reject a request by an exchange to consider an application for recognition of an enumerated anticipatory bona fide hedge. Proposed § 150.11(e)(1)(iii) delegated the Commission's authority to review any application for recognition of an enumerated anticipatory bona fide hedging position and delegate the authority to request related records or supporting information from the exchange or from the applicant.

Lastly, the Commission proposed in § 150.11(e)(iv), to delegate its authority to determine, under proposed § 150.11(d)(2), that it was not appropriate to recognize a commodity derivative position as an enumerated anticipatory bona fide hedging position, or that the disposition by an exchange of an application for such recognition is inconsistent with the filing requirements of proposed § 150.11(a)(2). The delegation also provided DMO with the authority, after any such determination was made, to grant the applicant a reasonable amount of time to liquidate its commodity derivative position or otherwise come into compliance.

This proposed delegation took into account that applications processed by an exchange under proposed § 150.11 would be for positions that should satisfy the requirements for enumerated bona fide hedging positions set forth in the Commission's rules, and should therefore be less likely to raise novel issues of interpretation, or novel issues with respect to consistency with the filing requirements of proposed § 150.11(a)(2), than applications processed under proposed § 150.9 or § 150.10. Such delegation is consistent with the Commission's longstanding delegation to DMO of its authority to review applications for recognition of enumerated bona fide hedging positions under current § 1.48, as well as consistent with the more streamlined approach to Commission review of enumerated anticipatory bona fide hedging position applications in proposed § 150.7.

Commission Reproposal

As noted above, the proposed processes under this rule are substantially similar to the corresponding provisions in § 150.9(f) and § 150.10(f). Hence, the Commission does not repeat the discussion of related comments here. The Commission is reproposing this rule, as originally proposed, for the reasons discussed above in connection with § 150.9(f), with the clarification that the Commission retains the authority to make the final determination to grant or deny hedge exemption applications.

*J. Miscellaneous Regulatory Amendments*

1. Part 150.6—Ongoing Application of the Act and Commission Regulations

Proposed Rule

The Commission proposed to amend existing § 150.6 to conform the provision with the general applicability of part 150 to SEFs that are trading facilities, and concurrently making non-substantive changes to clarify the provision. The provision, as amended and clarified, provides this part shall only be construed as having an effect on position limits and that nothing in part 150 shall affect any provision promulgated under the Act or Commission regulations including but not limited to those relating to manipulation, attempted manipulation, corners, squeezes, fraudulent or deceptive conduct, or prohibited transactions.[1189] For example, by requiring DCMs and SEFs that are trading facilities to impose and enforce exchange-set speculative position limits, the Commission does not intend for the fulfillment of such requirements alone to satisfy any other legal obligations under the Act and Commission regulations of DCMs and SEFs that are trading facilities to detect and deter market manipulation and corners. In another example, a market participant's compliance with position limits or an exemption does not confer any type of safe harbor or good faith defense to a claim that he had engaged in an

[1189] The Commission notes that amended § 150.6 matches vacated § 151.11(h).

attempted manipulation, a perfected manipulation or deceptive conduct.

Comments Received

The Commission received no comments on the proposed amendments to § 150.6.

Commission Reproposal

The Commission is reproposing § 150.6, with an amendment to clarify the application of part 150 to other provisions of the Act or Commission regulations. Specifically, in order to avoid any confusion regarding whether § 150.6 applies to position limits regulations found outside of part 150 of the Commission's regulations (*e.g.,* relevant sections of part 19), the amendment clarifies that recordkeeping and reporting regulations associated with speculative position limits are affected by part 150. The amendment also clarifies that regulations incorporated by reference to part 150 are also affected by the regulations promulgated under part 150. These changes, while not substantively different from the proposed rule, provide additional clarity regarding the application of part 150 to other provisions of the Act or Commission regulations.

The Commission also notes that § 150.6 applies despite the Commission's amendments to the appendices to parts 37 and 38 of the Commission's regulations regarding delayed implementation of exchange-set limits for swaps on exchanges without sufficient swaps position information.

2. Part 150.8—Severability

Proposed Rule

The Commission proposed to add § 150.8 to address the severability of individual provisions of part 150. Should any provision(s) of part 150 be declared invalid, including the application thereof to any person or circumstance, § 150.8 provides that all remaining provisions of part 150 shall not be affected to the extent that such remaining provisions, or the application thereof, can be given effect without the invalid provisions.[1190]

Comments Received

The Commission did not receive any comments regarding proposed § 150.8.

Commission Reproposal

The Commission is reproposing the severability clause in § 150.8. The Commission believes it is prudent to include a severability clause to avoid any further delay, as practicable, in carrying out Congress' mandate (underscored by the Commission's own preliminary finding of necessity) to impose position limits in a timely manner.

3. Part 15—Reports—General Provisions

Proposed Rule

The Commission proposed to amend the definition of the term ''reportable position'' in current § 15.00(p)(2) by clarifying that: (1) Such positions include swaps; (2) issued and stopped positions are not included in open interest against a position limit; and (3) special calls may be made for any day a person exceeds a limit. Additionally, the proposed amendments to § 15.01(d) added language to reference swaps positions and updated the list of reporting forms in current § 15.02 to account for new and updated series '04 reporting forms, as discussed above.[1191]

Comments Received

The Commission did not receive any comments regarding the proposed amendments to part 15.

Commission Reproposal

The Commission is reproposing amendments to part 15, as originally proposed, to update and clarify the definition of ''reportable position,'' add references to swaps positions, and add to the list of reporting forms.

4. Part 17—Reports by Reporting Markets, Futures Commission Merchants, Clearing Members, and Foreign Brokers

Proposed Rule

In the December 2013 Position Limits Proposal, the Commission proposed to amend current § 17.00(b) to delete provisions related to aggregation, since those provisions are duplicative of aggregation provisions in § 150.4.[1192] Instead, as proposed, § 17.00(b) provides that ''[e]xcept as otherwise instructed by the Commission or its designee and as specifically provided in § 150.4 of this chapter, if any person holds or has a financial interest in or controls more than one account, all such accounts shall be considered by the futures commission merchant, clearing member or foreign broker as a single account for the purpose of determining special account status and for reporting purposes.'' In addition, proposed § 17.03(h) delegates to the Director of the Division of Market Oversight or his designee the authority to instruct persons pursuant to proposed § 17.03.[1193]

Comments Received

The Commission did not receive any comments regarding the proposed changes to part 17.

Commission Reproposal

The Commission is reproposing amendments to part 17, as originally proposed, to delete duplicative aggregation provisions and delegate to the Division of Market Oversight the authority to instruct persons pursuant to proposed § 17.03.

4. Removal of Commission Regulations 1.47 and 1.48, and Part 151—Position Limits for Futures and Swaps

Proposed Rule

As discussed above, the Commission intended, in a 2011 final rule, to amend several other sections as part of its then adoption on part 151. Among the sections the Commission was then affecting was the removal and reservation of §§ 1.47 and 1.48. Both sections permitted market participants to seek recognition of positions as bona fide hedges.[1194]

However, prior to the compliance date for that 2011 rulemaking, as noted above, a federal court vacated most provisions of that rulemaking, including the amendments to the definition of a bona fide hedging position in § 1.3(z), as well as to the removal and reservation of §§ 1.47 and 1.48.[1195] Because the Commission did not instruct the **Federal Register** to roll back the 2011 changes to the CFR, the current CFR still shows the versions adopted in 2011, which shows §§ 1.47 and 1.48 as ''reserved.'' As the Commission noted in the December 2013 Position Limits Proposal, in light of the proposed amendments to part 150, as well as the District Court vacatur of part 151, the

[1190] The Commission notes that proposed § 150.8 matches vacated § 151.13.

[1191] *See* discussion of new and amended series '04 reports above.

[1192] In a separate final rulemaking, the Commission is finalizing amendments to § 150.4 regarding the aggregation of positions. *See* 2016 Final Aggregation Rule.

[1193] Previously, in 2013, the Commission adopted amendments to § 17.03. Ownership and Control Reports, Forms 102/102S, 40/40S, and 71, 78 FR 69178 (Nov. 18, 2013). The Commission is now proposing to amend § 17.03 further by adding § 17.03(h).

[1194] § 1.47 pertains to requirements for classification of purchases or sales of contracts for future delivery as bona fide hedging under § 1.3(z)(3 of the regulations, while § 1.48 addresses requirements for classification of sales or purchases for future delivery as bona fide hedging of unsold anticipated production or unfilled anticipated requirements under § 1.3(z)(2) (i)(B) or (i)(C) of the regulations.

[1195] *International Swaps and Derivatives Association* v. *United States Commodity Futures Trading Commission,* 887 F. Supp. 2d 259 (D.D.C. 2012).

amendments to the definition of a bona fide hedging position in 1.3(z), and the removal and reservation of §§ 1.47 and 1.48, the Commission again proposed to remove and reserve §§ 1.47 and 1.48.

Commission Reproposal

The Commission is reproposing to remove and reserve § 1.47 in light of the Commission's proposal of new provisions in § 150.9 addressing exchange recognitions of positions as non-enumerated bona fide hedging positions, subject to Commission review. Similarly, in connection with the reproposal of §§ 150.7 and 150.11, the Commission is proposing to remove and reserve, as originally proposed, § 1.48. Finally, the Commission is reproposing that part 151 be removed and reserved in response to the reproposed revisions to part 150 that conform it to the amendments made to the CEA section 4a by the Dodd-Frank Act.

## IV. Related Matters

### *A. Cost-Benefit Considerations*

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing certain orders. Section 15(a) further specifies that the costs and benefits 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 futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. The Commission considers the costs and benefits resulting from its discretionary determinations with respect to the Section 15(a) factors.

The baseline against which the Commission considers the benefits and costs of these reproposed rules is the statutory requirements of the CEA and the Commission regulations now in effect—in particular the Commission's Part 150 regulations and rules 1.47 and 1.48.[1196]

1. Necessity Finding

Out of an abundance of caution in light of the district court decision in *ISDA* v. *CFTC,*[1197] and without prejudice to any argument the Commission may advance in any forum, the Commission has preliminarily found, as a separate and independent basis for the Rule, that speculative position limits are necessary to achieve the purposes of the CEA.

a. Benefits of Speculative Position Limits Rules

The Commission expects that the speculative position limits in the reproposed Rule will promote market integrity. Willingness to participate in the futures and swaps markets may be reduced by perceptions that a participant with an unusually large speculative position could exert unreasonable market power. A lack of participation in these markets may harm liquidity, and consequently, may negatively impact price discovery and market efficiency as well.

Position limits may serve as a prophylactic measure that reduces market volatility due to large trades that impact prices. For example, a party who is holding large open interest may become unwilling or unable to meet a call for additional margin or take other steps that are necessary to maintain the position. In such an instance, the party may substantially reduce its open interest in a short time interval. In general, price impacts could arise from large positions as they are established or liquidated.

Exchanges and the Commission may gain insight into the markets as market participants seek exemptions from position limits. This may improve the exchanges' and the Commission's ability to supervise markets and to deter and prevent market manipulation. Further, the discipline of seeking exemptions that are tied to particular situations may improve a market participant's risk management practices, as it goes through the exercise of justifying the need for an exemption.

There are additional benefits to imposing position limits in the spot month. Spot month position limits are designed to deter and prevent corners and squeezes. Spot month position limits may also make it more difficult to mark the close of a futures contract to possibly benefit other contracts that settle on the closing futures price. Marking the close harms markets by spoiling convergence between futures prices and spot prices at expiration. Convergence is desirable, because it facilitates hedging of the spot price of a commodity at expiration. In addition, since many other contracts settle based on the futures price at expiration, mispricing could affect a larger scope of contracts.

b. Costs of Speculative Position Limits Rules

The Commission recognizes that position limits impose compliance costs on market participants. Under position limits, market participants must monitor their positions and have safeguards in place to remain under a federal position limit or an exemption level. Some market participants will have to incur the costs of seeking exemptions from federal positons limits. In this Reproposal, the Commission has sought to reduce these costs by setting the federal position limits at an appropriately high level and by relying on the experience and expertise of exchanges to administer exemptions.

Market participants who find position limits binding may have to transact in less effective instruments such as futures contracts that are similar but not the same as the core referenced futures contract. These instruments could include forward contracts, trade options, or futures on a foreign board of trade. Transacting in substitute instruments may raise transaction costs. Finally, if transactions shift to other instruments, futures prices might not reflect fully all the speculative demand to hold the futures contract, because substitute instruments may not influence prices in the same way that trading directly in the futures contract does. In these circumstances, futures market price discovery and efficiency might be harmed.

c. Summary of General Comments Regarding Speculative Position Limits Rules

i. Comments on General Aspects of the Rule

One commenter asserted that the proposed rules have the potential to increase systemic risk, impair market function, and increase the costs and volatility of wholesale energy commodities. Moreover, the commenter asserted that these adverse impacts are unrelated to any mandates placed upon the Commission by Congress.[1198]

Another commenter said that position limits that are not necessary or appropriate increase commercial parties' compliance costs and reduce market liquidity, which in turn increases the cost of hedging. The commenter believes the Commission did not adequately consider these costs and the lack of corresponding benefits.[1199]

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[1196] *See* December 2013 Position Limits Proposal, Table 4, at 75712, for a list of existing regulations related to enumerated bona fide hedges.

[1197] *International Swaps and Derivatives Association* v. *United States Commodity Futures Trading Commission,* 887 F. Supp. 2d 259 (D.D.C. 2012).

[1198] CL–IECAssn–59679 at 1–2.

[1199] CL–EEI–EPSA–59602 at 2 and 3, CL–EEI–Sup–60386 at 3.

One commenter requested that as the Commission enacts its final rule it should avoid imposing materially costly and complex rules and reporting requirements on hedgers unless they are manifestly necessary to prevent a meaningful threat to market integrity.[1200]

In response to 2016 Supplemental Position Limits Proposal RFC 37, a commenter stated that maintaining the status quo in which exchanges administer an established process for position limits and exemptions will provide legal certainty and maintain current costs instead of increasing them.[1201] In response to 2016 Supplemental Position Limits Proposal RFC 55, this commenter said that the Commission's Division of Enforcement has numerous tools at its disposal, and that the Exchanges have position step-down and exemption revocation authorization at their disposal, to enforce CEA market manipulation regulations.[1202]

Sen. Levin commented that the benefits of the proposed rules, while difficult to quantify, create a net benefit to the public and the markets by helping to ensure the markets' continued stability, fairness, and profitability.[1203]

ii. Response to Comments on General Aspects of the Rule

The Commission has interpreted the Dodd-Frank Act to mandate that the Commission impose federal position limits on physical-delivery futures contracts. In addition, the Commission is making a preliminary alternative finding that position limits are necessary to accomplish statutory objectives. The Commission believes that it has calibrated the levels of those limits so as to avoid harmful effects on the markets and, accordingly, does not believe the imposition of federal position limits at the reproposed levels will have the effects that concerned commenters. These commenter concerns are counterpoised by the desirable effects on markets that Sen. Levin ascribed to position limits.

iii. Comments on Cost Estimates

A commenter expressed concern that the CFTC has underestimated the costs of compliance with the position limits rules, and the number of affected parties, so that the potential unintended consequences of the rules will outweigh their benefits. The commenter believes this would result because the compliance costs associated with position limits are high and particularly burdensome for market participants who are unlikely ever to come close to reaching the limits.[1204]

Another commenter believes that the cost-benefit analysis in the 2016 supplemental proposal features unrealistically low estimates of the time and costs that will be required to implement and maintain compliance programs.[1205]

Another commenter asserted that the Commission did not adequately quantify the harm from position limits on liquidity for bona fide hedgers and the price discovery function, or the implementation and on-going reporting and monitoring costs for market participants. The commenter believes that costs will arise from altering speculative trading strategies in response to a limited definition of bona fide hedging; reassessing and modifying existing trading strategies to comply with limits; amending DCMs' current aggregation and bona fide hedging policies; and creating compliant application regimes for SEFs.[1206]

In response to 2016 Supplemental Position Limits Proposal RFC 56, another commenter asserted that unduly low position limits would reduce liquidity and discourage market participation, thereby not advancing regulatory goals that are already appropriately protected under the status quo. In response to 2016 Supplemental Position Limits Proposal RFC 66, this commenter said the Commission should consider public interest considerations relating to the particular interests of commercial end-users, which rely on mitigating price risk in order to remain in business. This commenter believes that commercial end-users are at risk of being squeezed out of the market, and potentially squeezed out of business, as a result of the difficulty of hedging commercial risks. The commenter urged the Commission to apply graduated regulatory requirements for bona fide hedging determinations that would account for differences between market participants.[1207]

iv. Response to Comments on Cost Estimates

As shown in the impact analysis, the Commission seeks to reduce market participants' compliance costs by setting the federal position limits at a level sufficiently high to only affect market participants with very large open interest. Thus, the Commission expects minimal compliance costs for those with positions below these high levels. Small traders would be required only to monitor their open interest and have safeguards in place to remain below position limits. The Commission finds the exemption process valuable because it requires participants with very large open interest to provide the information required by the exemption application to the relevant exchange(s) and to the Commission. Having this information helps exchanges and the Commission to better understand the markets they regulate.

As for the high costs that some commenters claimed to be required to implement and maintain compliance programs, the Commission presented and requested comment on its estimates of the costs associated with compliance programs. Commenters did not provide any specific cost estimates to support their assertions of the potential for high costs.

v. Comments on Cross-Border Aspects of the Rule

In response to 2016 Supplemental Position Limits Proposal RFC 67, a commenter noted that swaps and futures markets have become more global and suggested that restrictive position limit regulations and added reporting requirements would drive global companies to jurisdictions that have more friendly regulatory treatment.[1208] Another commenter urged the Commission to consider and assess the costs and benefits of applying the rules on an extraterritorial basis.[1209]

vi. Response to Comments on Cross-Border Aspects of the Rule

The Commission considers that market participants might use other means to engage in derivative activity besides domestic futures and swaps if federal position limits are set too low. For instance, price discovery for a futures contract might move to a foreign board of trade that lists a substitute contract. Further, foreign parties might elect to engage in foreign swaps instead of transacting in U.S. futures and swaps. To mitigate these risks, the Commission endeavors not to set the position limits at levels that are unduly low.

vii. Comments on Quantification of Costs of the Rule

A commenter criticized the Commission's consideration of the costs and benefits of the proposed rules for

[1200] CL–ASR–60933 at 5.

[1201] CL–IECAssn–60949 at 19.

[1202] CL–IECAssn–60949 at 23.

[1203] CL–Sen. Levin–59637 at 9–10.

[1204] CL–MFA–60385 at 12–13. *See also* CL–COPE–59622 at 5 and CL–CMC–59634 at 2.

[1205] CL–ISDA–60931 at 5.

[1206] CL–ISDA/SIFMA–59611 at 24–25.

[1207] CL–IECAssn–60949 at 23, 25–26.

[1208] CL–IECAssn–60949 at 26.

[1209] CL–ISDA/SIFMA–59611 at 23.

failing to consider both direct and indirect costs on commodities markets, market participants, and the economy generally.[1210] The Commenter believes that legal precedents require that in order to adopt a position limit rule, the Commission must find a reasonable likelihood that excessive speculation will pose a problem in a particular market, and that position limits are likely to curtail the excessive speculation without imposing undue costs.[1211] To the contrary, this commenter said it had not observed excessive speculation in the years since the financial crisis and, thus, position limits would only increase regulatory burdens with no corresponding benefit.[1212] Moreover, the commenter thinks the Commission did not adequately quantify the harm that market experts predict position limits will impose on liquidity for bona fide hedgers, the disruption to the price discovery function, or the shifting of price discovery offshore. The commenter also pointed to a lack of quantification of implementation costs, initial compliance and monitoring costs, and on-going reporting and monitoring costs for market participants, and the lack of quantified costs of a limited definition of bona fide hedging which would require alterations to speculative trading strategies to meet the definition; the amendments to DCMs' current aggregation and bona fide hedging policies; or the creation of compliant application regimes for SEFs.[1213]

The commenter cited papers by Craig Pirrong and Philip Verleger as proper evaluations of the costs and benefits of position limits for derivatives,[1214] and asserted that if quantitative information is lacking the Commission must make guesses, even if imprecise, and conduct an economic analysis of the likely impact of the proposed rules.[1215] In the paper cited by the commenter, Craig Pirrong suggested that the Commission could provide ''valuable evidence'' about costs and benefits by documenting for each commodity subject to limits, using a long period of historical data, how often limits would have been binding and how much large speculators would have had to reduce their positions in order to comply with limits.[1216] He believes it would be useful to see how often sudden and unreasonable price changes occurred during the period the limits would have been binding, in comparison to costs during periods when limits have been binding and not associated with sudden and unreasonable price changes.[1217] He said that a proper cost-benefit analysis should quantify net benefits relative to the status quo and identify which categories of market participants benefit, the sources of those benefits, and their magnitude, and also identify which types of participants are more likely to incur the costs associated with the limits, identify the sources of those costs, and quantify them, while providing the data and information necessary for replication of the analysis.[1218] Last, Mr. Pirrong believes the Commission should address potential costs raised by commenters on the position limit rules proposed in 2011.[1219]

Another commenter also thought that the Commission should perform a cost-benefit analysis to determine whether non-spot month position limits are justified. The commenter said that the Commission's statements that ''few'' participants would exceed the limits is not a sufficient analysis and that the Commission is obligated to do a more rigorous analysis before declaring 5, 7, or 11 persons as ''few.'' Further, the commenter pointed out that the Commission has not specifically stated how often those market participants would have exceeded those levels, how much over the limit they were, how the position exceedances were distributed along the price curve, or whether the positions were calendar spreads, and claimed that the lack of this information means there is no way to know whether the removal of those positions would have led to a significant reduction in liquidity and therefore market participants must assume that such a reduction in liquidity would have been significant.[1220]

Sen. Levin commented that the Commission correctly identified the prevention and reduction of artificial price disruptions to commodity markets as a positive benefit that would protect both market participants and the public, and that would outweigh the cost imposed on certain speculative traders. Sen. Levin commented that the Commission correctly observed that the sound risk management practices required by the proposed rules would benefit speculators, end users, and consumers.[1221] Sen. Levin believes these benefits would include: The promotion of prudent risk management (with Amaranth illustrating the dangers of poor risk management), and broader economic efficiency, public welfare, and political security attributable to the availability and price stability of commodities such as wheat.[1222]

viii. Response to Comments on Quantification of Costs of the Rule

The Commission does not believe that the consideration of costs and benefits under CEA section 15(a) requires a quantification of all costs and benefits. Nor does the statute require the Commission to hazard a guess when the available information is imprecise. The statute requires the Commission to consider the costs and benefits of its rulemaking, which contemplates a qualitative discussion when quantification is difficult.

The Commission addresses most of the commenter's cost and benefit concerns later in this consideration of costs and benefits. As for the identification and quantification of costs and benefits suggested by Mr. Pirrong, the Commission believes it would be of limited usefulness. For instance, the quantification would be highly uncertain and require many subjective interpretations and judgements on the part of investigators. Further, due to statutory restrictions on its release of confidential data, the Commission would be unable to provide data and other information necessary for the public to conduct an independent replication of the Commission's analysis.

The Commission considered proceeding in stages by first imposing

[1210] CL–ISDA/SIFMA–59611 at 3–4 and 22. *See also* CL–ISDA–60370 at 2.

[1211] CL–ISDA/SIFMA–59611 at 2, 3, *citing ISDA,* 887 F. Supp. 2d at 273. The commenter said the Commission should identify marginal benefits of the rule and evaluate the costs and benefits appropriately (given limitations on available data). *See also* CL–ISDA/SIFMA–59611 at 22, n. 83, *citing Inv. Co. Inst.* v. *CFTC,* 720 F.3d 370, 378–79 (D.C. Cir. 2013). Another commenter believed that the Commission must find there is a problem in market pricing as a result of positions exceeding non-spot month position limits, or a benefit from prohibiting such excess positions, before adopting position limits. CL–Working Group–59693 at 61. The commenter is concerned that, as a result of non-spot month position limits, parties carrying positions above the limit will lose the market opportunity experienced in holding the positions, there could be an immediate reduction in liquidity if those parties must liquidate those positions, and a reduction in the positions of the market participants would reduce open interest, reducing subsequent non-spot month limits and beginning a continuous downward cycle that eventually would draw liquidity from markets and impact hedgers. *Id.*

[1212] CL–ISDA/SIFMA–59611 at 30

[1213] CL–ISDA/SIFMA–59611 at 24–25

[1214] CL–ISDA/SIFMA–59611 at 22 fn 83

[1215] CL–ISDA/SIFMA–59611 at 23–24.

[1216] CL–ISDA/SIFMA–59611 at Annex B at 5.

[1217] CL–ISDA/SIFMA–59611 at Annex B at 5.

[1218] CL–ISDA/SIFMA–59611 at Annex B at 5–6.

[1219] CL–ISDA/SIFMA–59611 at Annex B at 6.

[1220] CL–Working Group–59693 at 61. The commenter also believes that non-spot month position limits would create a restraint on non-spot month liquidity due to strip positions along the curve, and this would create an unnecessary impact on hedgers. *Id.* at 61–62.

[1221] CL–Sen. Levin–59637 at 9.

[1222] CL–OSEC–59972 at 2.

position limits in the spot month before imposing then in the single month and all months combined. The Commission is preliminarily rejecting this alternative based on the impact analysis, because the single month and all months combined positon limits are set sufficiently high to impact only very few market participants. Further, the Commission believes that most of these participants would qualify for various exemptions to positions limits.

Another commenter asserted that the CEA directs the Commission to balance the four factors listed in CEA section 4a(a)(3)(B) and, thus, the Commission should present rigorous analysis to meet this requirement.[1223] In particular, the commenter pointed out that the Commission has not published an analysis of how the proposed position limits promote sound risk management and ensure that trading on foreign boards of trade in the same commodity will be subject to comparable limits so that position limits do not cause price discovery to shift to the foreign boards of trade.[1224]

In response to this commenter, the Commission interprets CEA section 4a(a)(3)(B) as a direction to the Commission to set limits ''to the maximum extent practicable'' to further the four policy objectives in that section. The Commission believes this is a Congressional recognition of the impossibility of achieving an actual ''maximum'' for each of the four policy objectives. In any case, as part of this consideration of costs and benefits, the Commission considers the promotion of sound risk management practices and whether price discovery in a commodity will shift to a foreign board of trade.[1225]

ix. Comments on Liquidity Effects

Commenters addressed the effects of position limits on liquidity. One expressed concern that the proposed position limits may constrain effective risk transfer by unduly restricting hedging or limiting the risk-bearing capacity of large speculators, thereby causing reduced liquidity, wider bid-offer spreads and higher transaction costs.[1226] Another thought the Commission did not consider that liquidity and price discovery may be diminished if speculative traders' activities are restricted.[1227] In response to 2016 Supplemental Position Limits Proposal RFC 62, another commenter said that price discovery will improve if market participants are allowed to innovate and grow without excessive governmental interference and regulatory reporting costs.[1228] And in response to 2016 Supplemental Position Limits Proposal RFC 59, this commenter suggested that position limits should be imposed in a manner that will foster innovation and growth for the betterment of the markets.

x. Response to Comments on Liquidity Effects

Liquidity is not a factor that the Commission is required to consider under section 15(a) of the CEA; nevertheless, the Commission did consider how liquidity concerns implicate the 15(a) factors. For instance, the Commission's regulatory goals generally include protecting market liquidity, and enhancing market efficiency and improving price discovery through increased liquidity. The Commission has sought to reduce market participant burdens with the understanding that regulatory compliance costs increase transaction costs, which might reduce liquidity, all else being equal. The Commission has considered that liquidity, including the risk-bearing capacity of markets, and price discovery may be harmed if position limits are set too low and so has sought to avoid these adverse effects.

The Commission preliminarily declines to treat general goals such as fostering innovation and growth for the betterment of markets as a specific public interest consideration under CEA section 15(a). While these are of course laudable objectives, the Commission believes they are difficult to accomplish through position limits. The Commission has not cited these general benefits as a reason for position limits. Last, the Commission notes that exchanges have proper incentives and a variety of tools with which to increase liquidity on their exchanges and, as a general matter, make their exchanges useful to the market.[1229]

xi. Comments Referring to Position Accountability

A commenter requested that the Commission compare the costs and benefits of the proposed position limits regime with those of a position accountability regime, because the commenter believed that position accountability levels would serve as a less costly and disruptive alternative to position limits.[1230] Another commenter compared a position accountability process to position limits, and argued that if the Commission imposes position limits for non-spot month contracts, the commenter would need to expend significant resources to ensure that its information technology systems could identify, gather and report bona fide hedging positions. But under position accountability, the commenter would be able to reply to a specific request for additional information using its own internal reports that have been designed to meet its specific commercial and risk-management needs. The position accountability approach would substantially reduce, if not eliminate, the burden of having to conform information technology systems to the Commission's reporting requirements.[1231]

A third commenter also suggested that while administering position accountability levels, the Commission could conduct a comprehensive cost-benefit analysis of the impact of spot month position limits on market liquidity for commercial hedgers and price discovery before determining whether to extend position limits outside of the spot months, and use the information collected to understand the trading activity of market participants with large speculative positions and determine if non-spot month

[1223] CL–CMC–59634 at 2.

[1224] *See*,CL–CMC–59634 at 3. *Cf.*CEA section 15(a)(2)(D) (titled ''Costs and Benefits''): ''The costs and benefits of the proposed Commission action shall be evaluated in light of . . . considerations of sound risk management practices;'' CEA section 4a(a)(2)(C) (titled ''Goal''): ''In establishing the limits required under [CEA section 4a(a)(2)(A)], the Commission shall strive to ensure that trading on foreign boards of trade in the same commodity will be subject to comparable limits and that any limits to be imposed by the Commission will note cause price discovery in the commodity to shift to trading on the foreign boards of trade.''

[1225] *See* the discussion of factors 3 (risk management) and 4 (price discovery) under section 15(a), below.

[1226] CL–MFA–60385 at 4.

[1227] *See* CL–ISDA/SIFMA–59611 at 25. Another commenter asserted that the Commission determined in 1993 that all-months-combined position limits are unnecessary and that the benefits of such limits did not outweigh the likely costs of eroding speculative volume and liquidity and the disruption in the efficient functioning of the non-storable commodity futures markets. CL–Working Group–59693 at 61 or CL–CMC. The commenter provided no citations to Commission actions in 1993. Commission staff believes that the commenter may be referring to a proposal from CME to eliminate the all-months-combined limits in the live cattle, live hogs, and feeder cattle futures and options markets in a March 4, 1993, submission. The Commission approved the proposal in an August 2, 1993, letter to the CME.

[1228] *See* CL–IECAssn–60949 at 24. Another commenter suggested that non-spot month position limits operate as a barrier to market entry for longer dated activities in the name of preventing ''a shallow threat'' of excessive speculation, and that costs resulting from position limits would be ultimately passed to the consumer, harming the American economy. CL–EDF–60398 at 4–5.

[1229] CL–Working Group–59693 at 61–62.

[1230] CL–MFA–60385 at 13.

[1231] CL–Calpine–59663 at 4.

speculative position limits are necessary.[1232]

xii. Response to Comments Referring to Position Accountability

The Commission considered administering position accountability levels in the non-spot month, but has preliminarily determined that the adoption of position limits with an exemption process is the better approach, because it benefits the supervisory functions of the exchanges and the Commission by providing better insight into the markets. In addition, the Commission notes it has a lack of statutory authority for the Commission itself to administer position accountability levels. Rather, the CEA authorizes exchanges to administer position accountability levels. In contrast, the Commission's emergency authority under the CEA is limited. Further, the Commission notes it interprets CEA section 4a(a)(3) as a direction to impose, at an appropriate level, position limits on the spot month, each other month (*i.e.,* single month), and the aggregate of all months.

2. DCM Core Principle 5(B) and SEF Core Principle 6(B), and new Appendix E to Part 150

a. Summary of Changes

*The Commission is reproposing to amend its guidance regarding DCM core principle* 5(B) and SEF core principle 6(B), and adopting a new Appendix E to Part 150. The amendments have the effect of delaying the implementation of exchanges' obligation to adopt swap position limits until there is sufficient access to swap position information regarding market participants' swap positions.

b. Baseline

The baselines for these changes are the Commission's current guidance on DCM Core Principle 5, SEF Core Principle 6, and the current Part 150.

c. Benefits and Costs

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its discretionary actions with respect to rules and orders. The Commission believes it is also appropriate to consider the costs and benefits of changes to the appendices to parts 37, 38, and 150 of the Commission's regulations, even though these appendices constitute guidance. The Commission appreciates that the changes to this guidance will delay the point in time when exchanges will become obligated to monitor and enforce federal position limits for swaps (although exchanges could take voluntary steps in this regard at any appropriate time). As a result, this change in guidance will likely confer benefits and reduce costs, although it is difficult to identify the benefits and costs that result directly from the change in guidance because the exact time at which exchanges will become obligated to monitor and enforce federal position limits for swaps is not currently specified but will instead depend on the future availability of information. Also, given the interrelationship between the exchanges' enforcement of federal position limits for swaps with the exchanges' other actions with respect to position limits and the Commission's enforcement of federal position limits, it is difficult to identify the incremental effect that will occur when exchanges become obligated to enforce federal position limits for swaps.

However, the Commission believes that because of the change in the Commission's guidance, exchanges and market participants will benefit because the delay will result in a lower requirement to invest in technology and personnel to assess federal position limits. In terms of costs, the Commission believes that there might be a cost to the market associated with this change in guidance because the delay may result in exchanges' reducing their monitoring of excessive positions in real-time.[1233]

d. Summary of Comments

The Commission requested comment on its consideration of the benefits and costs associated with the proposed amendments to guidance, and asked if there are additional alternatives that the Commission has not identified. Two commenters requested that the Commission formulate a plan to address the lack of data access by DCMs and SEFs.[1234] These commenters did not provide a detailed alternative, however. On the other hand, one commenter asserted that there should be no delay in implementing position limits for swaps because, according to the commenter, the Commission has access to sufficient swap data it needs to implement position limits.[1235] The Commission is considering various alternatives, but has not made a determination on which direction to take.

3. Section 150.1—Definitions

The Commission is reproposing new definitions of, or amendments to the definitions of, several terms: Basis contract, bona fide hedge, calendar spread contract, commodity derivative contract, commodity index contract, core referenced futures contract, eligible affiliate, entity, excluded commodity, futures-equivalent, intercommodity spread, long position, short position, spot month, intermarket spread, physical commodity, pre-enactment swap, pre-existing position, referenced contract, spread contract, speculative position limit, swap, swap dealer, and transition period. These new definitions and amendments are discussed above.

a. Benefits and Costs

A general benefit of including definitions in the regulation is greater clarity. In particular, having specific definitions of terms set out as a separate part of the regulations helps users of the regulation to understand how the position limit rulemaking relates, in general, to the concepts and terminology of CEA as amended by the Dodd-Frank Act. Although market participants and other users of the regulations must take time and effort to understand and adapt to new definitions in the context of the rulemaking, the Commission believes these costs are reduced by setting out the definitions as a separate part of the regulations rather than incorporating the definitions in the substantive provisions of the rules.

Specific benefits and costs of definitions are discussed within the context of specific rules where the definitions are directly applicable. In addition, the Commission believes that several definitions merit a specific consideration of costs and benefits, because the adoption of these definitions would represent the exercise of substantive discretion on the part of the Commission.

b. Bona Fide Hedging Position

i. Summary of Changes

The Commission is reproposing a definition of bona fide hedging position in § 150.1. The Commission believes this definition of bona fide hedging position is consistent with CEA section 4a(c) regarding physical commodities and otherwise closely conforms to the status quo. Commercial cash market activities are covered by the part of the definition that sets out an economically appropriate test. The Commission also notes that since CEA 4c(a)(5) separately states that intentional or reckless

[1232] CL–FIA–60303 at 3–4.

[1233] As stated in Section IIA, the Commission foresees various possibilities in remediating this current inability to monitor position limits in real-time in the future.

[1234] CL–AFR–60953 at 2; CL–RER2–60962 at 1.

[1235] CL–Better Markets–60928 at 6.

disregard for orderly trading execution is unlawful and because it is unclear how a market participant would comply with an orderly trading requirement in the context of OTC transactions, the Commission is proposing to delete the orderly trading requirement in the definition of bona fide hedging position. The Commission's addition of subparagraph (2)(iii)(C) to the definition of bona fide hedging position in § 150.1 reiterates the Commission's authority to permit exchanges to recognize bona fide hedging positions in accordance with § 150.9(a). Those positions are subject to CEA section 4a(c) standards as well as Commission review.

ii. Baseline

The baseline for this amendment to the rule is the definition for ''bona fide hedging transactions and positions,'' set forth in current § 1.3(z).[1236]

iii. Benefits and Costs

Futures contracts function to hedge price risk because they allow a party to fix a price for a specified quantity of a particular commodity at a designated point in time. Futures contracts, thereby, can be used by market participants to create price certainty for physically-settled transactions. Thus, the Commission believes that to qualify as a bona fide hedging position for a physical commodity, the position must ultimately result in hedging against some form of price risk in the physical marketing channel.

The Commission is amending the five day/spot month rule so that it will allow exchanges to grant spread exemptions that are valid in the five day/spot month period. The Commission anticipates that allowing spread exemptions to be recognized in the spot month might improve liquidity and, thereby, lower costs for market participants.

Also, the rule amendments will allow bona fide hedge exemptions to cover a period of more than one year of cash market exposure. The current definition limits to one year the hedging of anticipated production of, or requirements for, an agricultural commodity. Removing this current restriction is desirable because many commercial enterprises may prefer to hedge cash market exposure for more than one year.

The Commission understands that some activity that may have been recognized by exchanges as bona fide hedging in the past may not satisfy the definition in the reproposed rule. The Commission has sought to mitigate costs arising from this transition by setting position limits at levels that are appropriately high (so as to limit the extent of positions that may require an exemption) and by not including any requirement that exchanges use the reproposed rule's definition of bona fide hedging position other than with respect to the federal position limits in the referenced contracts listed in 150.2(d).

The Commission notes that an exchange is permitted to recognize exemptions for non-enumerated bona fide hedging positions, certain spread positions, and anticipatory bona fide hedging positions, under the processes of § 150.9, 150.10 and 150.11, respectively, subject to assessment of the particular facts and circumstances, where price risk arises as a result of other fact patterns than those of the enumerated positions. The Commission expects to review with an open mind any hedging activity that exchanges choose to exempt as bona fide hedging positions with respect to federal position limits. The Commission believes, however, that it would be inappropriate to allow the exchanges to act with unbounded discretion in interpreting the meaning of the term ''economically appropriate'' when the exchanges determine whether to recognize an exemption for bona fide hedging. Such a broad delegation is not authorized by the CEA and, in the Commission's view, would be contrary to the reasonably certain statutory standards in CEA section 4a(c), such as the ''economically appropriate'' test. That is, if the statutory standards are reasonable certain, then the Commission may delegate authority to exchanges. If the statutory standards were not reasonably certain, then the Commission would be precluded from delegating authority to the exchanges. Further, as explained in the discussion of § 150.9, 150.10 and 150.11, exchange determinations in this regard will be subject to the Commission's *de novo* review.

iv. Summary of Comments

Several commenters said that the rule's definition of bona fide hedging position should be expanded in various ways that would extend the scope of the definition to include the hedging of a wider variety of risks, in addition to price risk. For example, one commenter claimed that hedging some of the risks and costs associated with building energy infrastructure may not satisfy the bona fide hedging position definition, and that as a result some of these costs would likely be passed onto consumers.[1237] A commenter representing asset managers said that the final rule should include a risk management exemption, including for commodity index contract positions, because the availability of such an exemption would reduce compliance costs and reduce negative consequences for liquidity and price discovery, while providing the same benefit in terms of preventing excessive speculation.[1238] A third commenter asserted that the ''specifically enumerated'' criterion in the proposed definition would constrain risk management activities by effectively reclassifying large risk reducing positions as excessive speculation.[1239] On the other hand, a fourth commenter believed that the definition of bona fide hedging position in the supplemental proposal will benefit consumers through lower prices enabled by an efficient hedging mechanism as existing strategies remain readily available.[1240]

Another commenter asserted that the correlation standards in the proposed rule would make the bona fide hedging position exemption unavailable for hedges related to illiquid delivery locations and result in higher risks for market participants and higher costs for consumers.[1241] Along similar lines, another commenter said the Commission had not sufficiently considered the commonly accepted accounting practice of entering into economic hedges or sufficiently analyzed the costs and burdens to companies that engage in economic hedging of applying the 0.80 correlation for cross-commodity hedging required in the final rule.[1242]

The Commission believes that the definition of bona fide hedging position and the related exemption process in the reproposed rule will accommodate many existing hedging strategies that market participants use. As it would be impossible to enumerate every acceptable bona fide hedging activity, the Commission has preliminarily determined that it is appropriate to rely on the experience and expertise of exchanges to process these exemptions. The Commission believes that the exchanges will be better placed to

[1236] 17 CFR 1.3(z) (2010). As discussed above, a district court generally vacated the Commission's part 151 rulemaking, that would have amended § 1.3(z) to apply only to excluded commodities. However, the Commission has not instructed the **Federal Register** to roll back those vacated amendments. Thus, the current version of § 1.3(z) is found in the 2010 or earlier version of the CFR.

[1237] CL–Working Group–59693at 23–26.

[1238] CL–AMG–60946 at 2–3.

[1239] CL–CME–59718 at 47.

[1240] CL–NGFA–60941 at 2–3

[1241] *See, e.g.,* CL–EEI–EPSA–59602 at 14. The commenter believes that the Commission evaluated only correlation during the spot month, but not the closer correlation that typically exists in the non-spot months. *Id.*

[1242] CL–NRG at 5

determine which activities qualify for bona fide hedging position exemptions based on the applicable facts and circumstances. The Commission anticipates that the exchanges' role in administering bona fide hedging position exemptions will help to mitigate the potential adverse effects that commenters attributed to an overly narrow application of such exemptions.[1243]

Regarding commenters' suggestions that the definition of bona fide hedging position be expanded to encompass hedges of risks other than risks related to prices in physical marketing channels, the Commission notes that many risks come into play outside the physical marketing channel to which referenced contracts relate. The Commission has preliminarily determined that hedging of these other risks should not be covered by the bona fide hedging position definition, because the Commission views the statutory standards in CEA section 4a(c)(2), largely mirroring those of the general definition of a bona fide hedging position in § 1.3(z)(1), to be reasonably certain as limited to hedges of price risks. Further, as explained above, the statutory standard of CEA section 4a(c) requires bona fide hedging positions to be a substitute for a transaction taken or to be taken in the cash market. Generally, this precludes application of the bona fide hedging exemption to hedging of purely financial risks that are not price risks related to the physical marketing channel. For example, commodity index contracts are not eligible for recognition as the basis of a bona fide hedging position exemption because these contracts are not used to hedge price risks in physical marketing channels, as required in CEA section 4a(c)(2)(A)(i), and, as well, would not meet the requirements for a bona fide hedging position as a pass-through swap offset under CEA section 4a(c)(2)(B).

Commenters also addressed the element of the bona fide hedging position definition that generally requires that hedges be considered on a net basis in determining whether the definition is satisfied. One commenter argued that hedging on a net basis would be unworkable and require costly new technology systems to be built around more rigid, commercially impractical hedging protocols that prevent dynamic risk management in response to rapidly changing market conditions.[1244] Another commenter asserted that hedging on a gross basis is economically appropriate in a variety of circumstances and the Commission's proposal would limit market participants' ability to hedge the risks associated with their commercial activities, potentially resulting in increased costs and volatility that could detrimentally impact the market participants and lead to higher prices for consumers.[1245]

The Commission believes that it is fundamental to the definition of bona fide hedging position to require that such hedging reduce the overall risk of the commercial enterprise. Consistent with that focus on overall risk, it should be noted that the Commission does recognize certain gross hedges, *e.g.,* the use of a calendar month spread position to hedge the price risk of a soybean crush processor, because those gross hedges reduce overall risk. That is, in applying the definition one must consider whether a hedge reduces the overall risk of the commercial enterprise, and overall risks must be determined on a net basis.[1246] In this aspect, too, the Commission believes that the involvement of exchanges in the bona fide hedge exemption process will be valuable, and the Commission would expect to consider the determinations of exchanges in this regard with an open mind.

Four commenters expressed opposition to an aspect of the proposal in the supplemental notice that would not allow hedge exemptions for spread transactions to be applied during the last five days of trading of a futures contract, saying that spread exemptions should be allowed into the spot month to avoid negative effects on liquidity and potential disruptions of convergence, potentially resulting in additional risk for market participants which ultimately gets passed to consumers.[1247]

The Commission agrees with commenters that allowing spread exemptions to be applied in the spot month might improve liquidity and lower risks for market participants. Thus, the Reproposal would permit exchanges to grant § 150.10 spread exemptions into the five day/spot period. The costs and benefits of the forms are considered in the discussion of Part 19 and rule 150.7.

*c. Core Referenced Futures Contract and Referenced Contract*

i. Summary of Changes

The Commission proposes to define the term ''core referenced futures contract'' and amend the list of contracts in § 150.2. The effect of this is that the federal positon limits in § 150.2(d) will apply to the following additional contracts: Rough Rice, Live Cattle, Cocoa, Coffee, Frozen Orange Juice, U.S. Sugar No. 11, U.S. Sugar No. 16, Light Sweet Crude Oil, NY Harbor ULSD, RBOB Gasoline, Henry Hub Natural Gas, Gold, Silver, Copper, Palladium, and Platinum.

ii. Baseline

The baseline for the definition of the term ''core referenced futures contract'' is that the term encompasses the legacy agricultural futures contracts that are subject to existing federal position limits, namely: Corn (and Mini-Corn), Oats, Soybeans (and Mini-Soybeans), Wheat (Mini-Wheat), Soybean Oil, Hard Winter Wheat, Hard Red Spring Wheat, and Cotton No. 2. The baseline for the definition of the term ''referenced contract'' is the same as that of the term ''core referenced futures contract.''

iii. Benefits and Costs

The definitions of the terms ''core referenced futures contract'' and ''referenced contract'' set the scope of contracts to which federal position limits apply. As noted above, the Commission has preliminarily decided to proceed in stages when imposing federal position limits. Among other things, this will allow the Commission to observe how futures markets respond to an initial set of position limits before applying position limits more widely, including to contracts with less liquidity. All other things being equal, markets for contracts that are more illiquid tend to be more concentrated, so that a position limit on such contracts might significantly reduce trading interest on one side of the market, because a large trader would face the potential of being capped out by a position limit. For this reason, among others, the contracts to which the position limits in § 150.2(d) apply include some of the most liquid physical-delivery futures contracts. Following the application of position limits to these contracts, the Commission would be able to study the effects of position limits more readily and, it is anticipated, consider how to apply position limits more broadly in a

[1243] For example, the Commission believes that the exchanges' involvement in this process is more flexible and far superior to setting out regulatory safe harbors for factors such as a linear correlation in the spot month that may demonstrate a position qualifies for the exemption.

[1244] *See, e.g.,* CL–EEI–EPSA–59602 at 15, CL–EEI–Sup–60386 at 7. *See also* CL–Calpine–59663 at 7.

[1245] CL–Olam–59946 at 1.

[1246] *See* the Commission determination regarding comments on specific, identifiable risks, above, for an explanation of why it would be inappropriate to apply the bona fide hedging definition on an item by item basis.

[1247] *See* CL–NCGA–ASA–60917 at 7; CL–IECAssn–60949 at 25; and CL–FIA–60937 at 18–19.

way that would not unduly restrain liquidity in less liquid markets.

The Commission has also preliminarily determined not to apply position limits to cash-settled core referenced futures contracts (that are not linked to physical-delivery futures contracts) at this time. For these contracts, the possibility of corners and squeezes is reduced, because there is no link to a physical-delivery futures contract that may be distorted, and therefore there is less of a need for position limits. Of course, there may be other concerns about manipulation of cash-settled futures contracts that are not linked to physical-delivery futures contracts, however. For instance, there may be an incentive to manipulate a commodity price index in a manner that would benefit particular cash-settled futures or swap positions. Such manipulative conduct includes cornering or squeezing the underlying cash market on which a cash-settlement index is based. The Commission notes that these manipulation concerns may be addressed, in part, through the Commission's authority to regulate futures and swaps (including the terms of these contracts set by exchanges) and take enforcement actions, until such time as the Commission adopts position limits on cash-settled core referenced futures contracts. Further, exchanges in their SRO function may also constrain and discipline traders who are trading in a disruptive fashion. Indeed, it is reasonable to expect that, given the exchanges' deep familiarity with their own markets and their ability to tailor a response to a particular market disruption, such exchange action is likely to be more effective than a position limit in such circumstances. However, the Commission notes the exchanges do not have authority over those persons who only transact in OTC swaps.

The Commission has preliminarily determined to exclude trade options from the rule's definition of ''referenced contract,'' for several reasons. The Commission believes that many trade options would qualify for bona fide hedging position exemptions, since trade options are generally used to hedge risks. The Commission also believes that not including trade options in the scope of position limits will relieve many market participants of significant compliance costs that would be required to apply position limits to trade options. Last, this approach will allow the market to continue to innovate in the use of trade options to hedge a variety of risks.

The rule's definition of the term ''referenced contract'' includes a swap or futures contract that is ''indirectly linked'' to a physical-delivery futures contract. The ''indirectly linked'' contract could be a cash-settled swap or cash-settled futures contract that settles to the price of another cash-settled derivative that, in turn settles to the price of a physical-delivery futures contract. A contract that settles based on the level of a commodity price index, comprised of commodities that are not the same or substantially the same, would not be an ''indirectly linked'' contract, even if the index uses futures prices as components. A contract based on such a commodity price index is excluded because the index represents a blend of the prices of various commodities.

The Reproposal's definition of the term ''referenced contract'' does not include a swap or futures contract that fixes its closing price on the prices of the same commodity at different delivery locations than specified in the core referenced futures contract, or on the prices of commodities with different commodity specifications than those of the core referenced futures contract. This approach is also in accord with market practice, in that a core referenced futures contract specifies location(s) and grade(s) of a commodity in the relevant contract specification. Thus, a contract on one grade of commodity is treated by the market as different from a contract on a different grade of the same commodity.

A location basis contract—a contract which reflects the difference between two delivery locations of the same commodity—is also excluded from the definition of referenced contract.[1248] A location basis contract may be used to hedge price risks relating to delivery at a location other than that of the core referenced futures contract. For instance, a location basis contract can be used in combination with a referenced contract to create a synthetic derivative contract on a commodity at a different delivery location, with a resulting zero net position in the referenced contract. However, a location basis contract that had a relatively small difference in location with that of the core referenced futures contract likely would not expose a speculator to significant price risk. Absent the exclusion of location basis contracts from the definition of referenced contract, such a speculator could increase exposure to a referenced contract by netting down, using such a location basis contract, the position that would otherwise be restricted by a position limit on the referenced contract.

iv. Summary of Comments

Commenters said that trade options should not be included in the definition of ''referenced contract.'' One commenter said there is significant uncertainty about the distinction between forward contracts and trade options, so costs associated with imposing position limits on trade options would greatly exceed any benefits.[1249] Another argued that because trade options have never been subject to position limits, commercial parties do not have any systems in place to: Distinguish between trade options that are referenced contracts and those that are not; monitor the number and quantity of referenced-contract trade option positions across delivery points and trading venues; and integrate them with other position tracking systems.[1250]

The Commission took the difficulties explained by commenters in complying with position limits on trade options into account when preliminarily determining not to include trade options in the definition of referenced contract. To provide flexibility, the reproposed rule permits trade options to be taken into consideration as a cash position, on a futures-equivalent basis, as the basis of a bona fide hedging position.

Another commenter discussed the exclusion of commodity index swaps from the definition of swaps that are economically equivalent to core referenced futures contracts. This commenter said this disparate treatment will shift trading activity to index swaps, drain liquidity from exchange-listed products, harm pre-trade transparency and the price discovery process, and further depress open interest (as volumes shift to index swap positions that do not count toward open interest calculations).[1251]

[1248] The defined term ''location basis contract'' generally means a derivative that is cash-settled based on the difference in price, directly or indirectly, of (1) a core referenced future contract; and (2) the same commodity underlying a particular core referenced futures contract at a different delivery location than that of the core referenced futures contract.

[1249] CL–FIA–59595 at 20.

[1250] *See, e.g.,* CL–NGSA–59674 at 33; CL–NGSA–59900 at 9. Another commenter made a more general assertion that the costs of monitoring positions subject to a limit, including reporting costs, would drive commercial market participants to the spot markets and cause them to restrict the variability provided to customers, if trade options or forward contracts with optionality were subject to position limits. CL–Calpine–59663 at 5.

[1251] CL–Citadel–59933 at 1–3. The commenter also made two recommendations relevant to the definition of core referenced futures contract: That position limits for cash-settled contracts are not warranted and that commodity index swaps should

Continued

The Commission acknowledges uncertainty about whether there will be a loss in liquidity due to the imposition of federal position limits. The Commission will monitor this issue going forward.

Another commenter suggested that the definition of bona fide hedging position should include the hedging of a binding and irrevocable bid, because a failure to do so could increase the costs incurred by utilities and special entities to provide power or gas by forcing bidders to incorporate into their bids or offers the cost associated with the risk that no exemption for such a hedge would be permitted.[1252] In response, the Commission points out that, under reproposed § 150.9, a bidder may seek recognition of a non-enumerated bona fide hedging position, under which an exchange may consider the facts and circumstances on a case-by-case basis.

d. Futures Equivalent

i. Summary of Changes

The Commission is reproposing two further revisions to the definition of ''futures-equivalent'' in the rule. The first revision clarifies that the term ''futures-equivalent'' includes a futures contract which has been converted to an economically equivalent amount of an open position in a core referenced futures contract. Second, the Commission clarifies that, for purposes of calculating futures equivalents, the size of an open position represented by an option contract must be determined as the economically-equivalent amount of an open position in a core referenced futures contract.

ii. Baseline

The baseline for this change to the rule's definition of ''futures equivalent'' is the current § 150.1(f) definition of ''futures-equivalent''.

iii. Benefits and Costs

The Commission has preliminarily determined that the definition of ''futures-equivalent'' in current § 150.1(f) is too narrow in light of the Dodd-Frank Act amendments to CEA section 4a. To conform to the statutory changes and to make the definition more amenable to application within the broader position limits regime, the Commission is reproposing a more descriptive definition of the term ''futures-equivalent'' by adding more explanatory text. The Commission continues to believe that, as it stated in the proposal, there are no cost or benefit implications to these further clarifications.

iv. Summary of Comments

The Commission requested comment on the revisions to the definition of the term ''futures equivalent,'' but did not receive any substantive comments. Consequently, the Commission is reproposing the definition in the Supplemental 2016 position limit proposal.

e. Intermarket Spread Position and Intramarket Spread Position

i. Summary of Changes

Current part 150 does not contain definitions for the terms ''intermarket spread position'' or ''intramarket spread position.'' In the Supplemental 2016 Position Limits Proposal the Commission proposed to expand the scope of definitions of these terms that had been included in the December 2013 Position Limits Proposal. The expanded definitions of ''intermarket spread position'' or ''intramarket spread position'' include positions in multiple commodity derivative contracts. This expansion would allow market participants to establish an intermarket spread position or an intramarket spread position that would be taken into account under the position limits regime and exemption processes. The expanded definitions also cover spread positions established by taking positions in derivative contracts in the same commodity, in similar commodities, or in the products or by-products of the same or similar commodities.

ii. Baseline

Current § 150.1 does not include definitions for the terms ''intermarket spread position'' and ''intramarket spread position.'' Therefore, the baseline is a market where ''intermarket'' and ''intramarket'' spread positions are not explicitly included in the definition of contracts that are exempt from federal position limits.

iii. Benefits and Costs

The changes to the definitions of the terms ''intermarket spread position'' and ''intermarket spread positions'' broaden the scope of the two terms in comparison to the definitions proposed in the December 2013 Position Limits Proposal. In the Commission's view, the changes are only operative in the application of §§ 150.3, 150.5 and 150.10, which address exemptions from position limits for certain spread positions. The two definitions operate in conjunction with § 150.10, which sets forth a process for exchanges to administer spread exemptions. The definitions and § 150.10, together, will enable market participants to obtain relief from position limits for these types of spreads, among others.

iv. Summary of Comments

Citadel recommended that cross-commodity netting should be permitted.[1253] The Commission preliminarily declines to permit cross-commodity netting within a particular referenced contract. However, the Commission addresses cross-commodity netting in the context of authorizing exchanges to recognize spread exemptions under reproposed § 150.10.

4. Section 150.2—Speculative Position Limits

a. Rule Summary

As previously discussed, the Commission interprets CEA section 4a(a)(2) to mandate that it establish speculative position limits for all agricultural and exempt physical commodity derivative contracts and, as a separate and independent basis for this rulemaking, has made a preliminary finding that position limits are necessary as a prophylactic measure to carry out the purposes of section 4a(a).[1254] The Commission currently sets and enforces speculative position limits for futures and futures-equivalent options contracts on nine agricultural products. Specifically, current § 150.2 provides ''[n]o person may hold or control positions, separately or in combination, net long or net short, for the purchase or sale of a commodity for future delivery or, on a futures-equivalent basis, options thereon, in excess of [enumerated spot, single-month, and all-month levels for nine specified contracts].'' [1255] The Commission proposed to amend § 150.2 to expand the scope of federal position limits regulation in three chief ways: (1) Specify limits on 16 contracts in addition to the nine existing legacy contracts (*i.e.,* a total of 25); (2) extend the application of these limits beyond futures and futures-equivalent options to all commodity derivative interests, including swaps; and (3) extend the application of these limits across trading venues to all economically equivalent contracts that are based on the same

not be treated differently than other cash-settled contracts: *Id.*

[1252] *See, e.g.,* CL–EEI–EPSA–59602 at 18.

[1253] CL–Citadel–59933 at 4.

[1254] *See supra* discussion of the Commission's interpretation of this mandate and the alternative necessity finding.

[1255] These contracts are Chicago Board of Trade corn and mini-corn, oats, soybeans and mini-soybeans, wheat and mini-wheat, soybean oil, and soybean meal; Minneapolis Grain Exchange hard red spring wheat; ICE Futures U.S. cotton No. 2; and Kansas City Board of Trade hard winter wheat.

underlying commodity. In addition, the Commission's proposed rule included methods and procedures for implementing and applying the expanded limits.

The Commission is reproposing amendments to § 150.2 to impose speculative position limits as mandated by Congress in accordance with the statutory bounds that define the Commission's discretion in doing so and, as a separate and independent basis for the Reproposal, because the speculative position limits are necessary to achieve their statutory purposes.[1256] First, pursuant to CEA section 4a(a)(5) the Commission must concurrently impose position limits on swaps that are economically equivalent to the agricultural and exempt commodity derivatives for which position limits are mandated in CEA section 4a(a)(2), and for which the Commission separately finds position limits are necessary. Second, CEA section 4a(a)(3) requires that the Commission appropriately set limit levels mandated and/or found necessary under section 4a(a)(2) that ''to the maximum extent practicable, in its discretion,'' accomplish four specific objectives.[1257] Third, CEA section 4a(a)(2)(C) requires that in setting limits mandated (or adopted as necessary) under section 4a(a)(2)(A), the ''Commission shall strive to ensure that trading on foreign boards of trade in the same commodity will be subject to comparable limits and that any limits. . . imposed. . .will not cause price discovery in the commodity to shift to trading on the foreign boards of trade.'' Key elements of the reproposed rule are summarized below.[1258]

Generally, § 150.2 will limit the size of speculative positions,[1259] *i.e.,* prohibit any person from holding or controlling net long/short positions above certain specified spot month, single month, and all-months-combined position limits. These position limits will reach: (1) 25 ''core referenced futures contracts,''[1260] representing an expansion of 16 contracts beyond the 9 legacy agricultural contracts identified currently in § 150.2;[1261] (2) a newly defined category of ''referenced contracts'' (as defined in § 150.1);[1262] and (3) across all trading venues to all economically equivalent contracts that are based on the same underlying commodity.

b. § 150.2(a) Spot-Month Speculative Position Limits

i. Summary of Changes

In order to implement CEA section 4a(a)(3)(A), reproposed rule § 150.2(a) prohibits any person from holding or controlling positions in referenced contracts in the spot month in excess of the level specified by the Commission for referenced contracts.[1263] Additionally, § 150.2(a) requires that a trader's positions, net long or net short, in the physical-delivery referenced contract and linked cash-settled referenced contract be calculated separately under the spot month position limits fixed by the Commission for each. As a result, a trader could hold positions up to the applicable spot month limit in the physical-delivery contracts, as well as positions up to the applicable spot month limit in linked cash-settled contracts (*i.e.,* cash-settled futures and swaps), but would not be able to net across physical-delivery and cash-settled contracts in the spot month.

ii. Baseline

To the extent the Commission has correctly interpreted that CEA section 4a(a)(2) mandates position limits, the costs and benefits of whether to require position limits have been balanced by Congress and the Commission is not tasked with revisiting those costs and benefits on that specific question.[1264] To the extent the Reproposal rests on the preliminary alternative necessity finding, the baseline is the current § 150.2 of the Commission's regulations.

iii. Benefits and Costs

As discussed above, CEA section 4a(a)(3)(A) directs the Commission, each time it establishes limits, to set limits on speculative positions during the spot-month.[1265] It is during the spot-month period that concerns regarding certain manipulative behaviors, such as corners and squeezes, become most urgent.[1266] The Commission has for decades applied guidance that spot-month position limits for physical-delivery futures contracts should be equal to no more than one-quarter of the estimated deliverable supply for that commodity. Spot-month position limits provide benefits to the market by restricting speculators' ability to amass market power, regardless of whether there is intent to manipulate or distort the market. In so doing, spot-month position limits restrict the ability of speculators to engage in corners and squeezes and other forms of manipulation. They also prevent the potential adverse impacts of unduly large positions even in the absence of manipulation, thereby promoting a more orderly liquidation process for each contract and fostering convergence between the expiring core referenced futures contract and its underlying cash market. This makes the core referenced futures contract more useful for hedging cash market positions.

For example, as discussed above, the absence of manipulative intent behind excessive speculation does not preclude the risk that accumulation of very large positions will cause the negative

[1256] *See supra* discussion of the Commission's necessity finding.

[1257] These objectives are to: (1) ''diminish, eliminate, or prevent excessive speculation;'' (2) ''deter and prevent market manipulation, squeezes, and corners;'' (3) ''ensure sufficient market liquidity for bona fide hedgers;'' and (4) ''ensure that the price discovery function of the underlying market is not disrupted.'' 7 U.S.C. 6a(a)(3).

[1258] For a more detailed description, *see* discussion above.

[1259] § 150.1 includes a definition of the term ''speculative position limits.''

[1260] § 150.1 defines the term ''core referenced futures contract'' by reference to ''a futures contract that is listed in § 150.2(d).''

[1261] Specifically, in addition to the existing 9 legacy agricultural contracts now within § 150.2—*i.e.,* Chicago Board of Trade corn (C), oats (O), soybeans (S), soybean oil (SO), soybean meal (SM), and wheat (W); Minneapolis Grain Exchange hard red spring wheat (MWE); ICE Futures U.S. cotton No. 2 (CT); and Kansas City Board of Trade hard winter wheat (KW)—proposed § 150.2 would expand the list of core referenced futures contracts to capture the following additional agricultural, energy, and metal contracts: Chicago Board of Trade Rough Rice (RR); ICE Futures U.S. Cocoa (CC), Coffee C (KC), FCOJ–A (OJ), Sugar No. 11 (SB) and Sugar No. 16 (SF); Chicago Mercantile Exchange Live Cattle (LC); Commodity Exchange, Inc., Gold (GC), Silver (SI) and Copper (HG); and New York Mercantile Exchange Palladium (PA), Platinum (PL), Light Sweet Crude Oil (CL), NY Harbor ULSD (HO), RBOB Gasoline (RB) and Henry Hub Natural Gas (NG). The Commission originally proposed in its 2013 to set position limits on 28 core referenced contracts, including the 25 contracts noted above plus CME Feeder Cattle, Lean Hog and Class III Milk. Those three contracts will not be included in the Reproposal for the reasons discussed above.

[1262] This would result in the application of prescribed position limits to a number of contract types with prices that are or should be closely correlated to the prices of the 25 core referenced futures contracts—*i.e.,* economically equivalent contracts—including: (1) ''look-alike'' contracts (*i.e.,* those that settle off of the core referenced futures contract and contracts that are based on the same commodity for the same delivery location as the core referenced futures contract); (2) contracts based on an index comprised of one or more prices for the same delivery location and in the same or substantially the same commodity underlying a core referenced futures contract; and (3) inter-commodity spreads with two components, one or both of which are referenced contracts.

[1263] As discussed *supra,* the Commission is reproposing to adopt a streamlined, amended definition of ''spot month'' in § 150.1. The term is defined as the trading period immediately preceding the delivery period for a physical-delivery futures contract and cash-settled swaps and futures contracts that are linked to the physical-delivery contract. The definition provides that the spot month for cash-settled contracts is that same period as that of the core referenced futures contract. For more details, *see* discussion above.

[1264] *See Nat'l Ass'n of Mfrs.* v. *SEC,* 748 F.3d 359, 369–70 (D.C. Cir. 2014).

[1265] 7 U.S.C. 6a(a)(3)(A).

[1266] *See* discussion above.

consequences of the types observed in the Hunt and Amaranth incidents. Moreover, it is often difficult to discern manipulative intent. That is one reason position limits are valuable as a prophylactic measure for, in the language of Section 4a(a)(1), ''preventing'' burdens on interstate commerce. The Hunt brothers and Amaranth examples illustrate the burdens on interstate commerce of excessive speculation that occurred in the absence of position limits, and position limits would have restricted those traders' ability to cause unwarranted price movement and market volatility. This would be so even had their motivations been innocent. Both episodes involved extraordinarily large speculative positions, which the Commission has historically associated with excessive speculation.[1267]

Exchanges and market participants also benefit from spot-month position limits because market participants who seek exemptions to the spot-month limit will have to justify why their positions qualify for the exemption, which fosters visibility into the market for the exchanges and fosters better risk management practices for the market participant seeking the exemption.

In its determination of the appropriate spot month levels for the core referenced futures contracts, the Commission took into account exchange estimates of deliverable supply, which were verified by the Commission staff, and exchange spot-month limit level recommendations. A more detailed discussion of the costs and benefits for the actual limits can be found below in the discussion of 150.2(d). However, more generally, the Commission recognizes federal spot month position limits do impose costs to exchanges and market participants. Federal spot month limits will require hedgers to apply for exemptions if they hold positions in excess of the federal limits. These costs are considered in the discussion of 150.3. In addition, speculators who want exposure beyond the federal limit for a referenced contract will incur costs to trade in instruments that are not subject to federal limits, such as trade options and bespoke swaps, which typically incur more expensive transactions costs than exchange traded futures and swaps.

Furthermore, as discussed above, exchanges may choose to adopt spot-month limits below the federal limit. Market participants who are hedging their cash market positions would incur costs of having to apply for an exemption from the exchange if their hedging positons are above the lower limit set by the exchange. Otherwise, a market participant who wants speculative exposure above the lower limit, but who does not qualify for an exemption, would have to take speculative positions in other instruments not subject to exchange or Federal position limits, which as noted above may involve higher transaction costs.

The Commission also recognizes that there are costs to setting federal spot-month limits too high or too low. If the Federal spot-month limit is too high, the exchanges and the Commission lose visibility into market activity because the number of exemption applications from market participants will be reduced because of the higher limit. In addition, if limits are too high, market participants could obtain positions that would impact the price of the commodity, possibly manipulating or distorting the futures price, thus impairing the price discovery process of the core referenced futures contract. Furthermore, if a market participant establishes a very large position and then has to unwind its position, there could be an adverse impact on the price of the core referenced futures contract (*e.g.,* as occurred with Amaranth).

Conversely, if the Federal spot-month limit is too low, market participants and exchanges would incur larger costs to apply for and process, respectively, more exemption applications. In addition, as noted above, transactions costs for market participants who are near or above the limit would rise as they transact in other instruments with higher transaction costs to obtain their desired level of speculative positions. Additionally, limits that are too low could incentivize speculators to leave the market and not be available to provide liquidity for hedgers, resulting in ''choppy'' prices and reduced market efficiency.[1268] Further, option premiums would likely increase to account for the more volatile prices of the underlying core referenced futures contract. Moreover, if confidence in the price of the core referenced futures contract erodes, market participants may move to another DCM or FBOT.

The Commission proposes to use its discretion in the manner in which it implements the statutorily-required spot-month position limits so as to achieve Congress's objectives in CEA section 4a(a)(3)(B)(ii); that is, to prevent or deter market manipulation, including corners and squeezes. For example, the Commission proposes to use its discretion under CEA section 4a(a)(1) to set limits that are equal in the spot-month for physical-delivery and linked cash-settled referenced contracts respectively. By setting separate limits for physical-delivery and cash-settled referenced contracts, the Reproposal restricts the size of the position a trader may hold or control in cash-settled referenced contracts, thus reducing the incentive of a trader to manipulate the settlement of the physical-delivery contract in order to benefit positions in the cash-settled referenced contract. Thus, the separate limits further enhance the prevention of market manipulation provided by spot-month position limits by reducing the potential for incentives to engage in manipulative action.

iv. Summary of Comments

One commenter urged the Commission to ensure that a final rule does not compromise predictable convergence in the market, or risk threatening the utility of contracts for risk management purposes, noting the importance of risk management to the general health of the economy.[1269] Another commenter noted the requirement that the Commission consider alternatives and said that the Commission should consider not adopting non-spot-month limits, limits that are set arbitrarily, or limits on financially settled contracts; consider recognizing cross-commodity netting; consider a plan for cross-border application of position limits; and consider new data sources, including SDRs (although such data's reliability is still in development).[1270]

The Commission agrees that the federal position limit regime should not unnecessarily impede convergence between the futures and cash markets, which would impede the price discovery process of the core referenced contract. As discussed below, the Commission endeavors to take into account how the position limit levels would impact the number of market participants in all of the referenced contracts to reduce undesirable impact on those markets.

The Commission has preliminarily exercised its discretion in determining how to adopt position limits and has chosen to start with the 25 core referenced futures contracts which were selected on the basis that such contracts:

[1267] December 2013 Position Limits Proposal, 78 FR 75685 n. 60.

[1268] ''Choppy'' prices often refers to illiquidity in a market where transacted prices bounce between the bid and the ask prices. Market efficiency may be harmed in the sense that transacted prices might need to be adjusted for bid-ask bounce to determine the fundamental value of the underlying contract.

[1269] CL–ADM–60300 at 3.

[1270] CL–ISDA/SIFMA–59611 at 26.

(1) Have high levels of open interest and significant notional value; or (2) serve as a reference price for a significant number of cash market transactions. The specific levels are not set arbitrarily. Rather, as discussed more below, the Commission takes into account the expertise of the exchanges that list the core referenced futures contracts. In that regard, the Commission received and verified estimates of deliverable supplies for core referenced futures contracts and considered spot-month limit levels those exchanges suggested. Regarding the data considered in setting the levels of non-spot month limits, Commission staff has worked with industry to improve the reliability of swap data collected pursuant to part 20 of Commission regulations. As discussed below in more detail, the Commission's confidence in the data has improved such that it relied on part 20 swap position data, to propose initial levels of federal non-spot month limits on futures and swaps in the Reproposal. The Commission addresses cross-commodity netting in the spread exemptions covered in reproposed § 150.10.

A commenter was concerned that the proposed position limits will cause market participants to transact in less-transparent and non-cleared markets due to a lack of liquidity on futures markets, and undermine efforts to encourage market transparency and reduce systemic risks through centralized clearing.[1271] Another commenter pointed out that constraining speculation would constrain hedging, and that more financial involvement in commodity markets has lowered risk premia and made hedging cheaper, making it economical to hold larger inventories that help reduce the frequency and severity of large price increases.[1272] A third commenter questioned whether the Supplemental Proposal's cost-benefit analysis includes the costs of processing bona fide hedging and spread exemptions for contracts subject only to exchange-set speculative position limits and not federal speculative position limits.[1273]

The Commission has preliminarily considered how the limits would impact traders. In that regard the Commission sought not to impede the liquidity of the markets for both hedgers and speculators by setting the spot month position limit at a level that would not deter hedgers or speculators from participating in the market. The Commission is mindful of the beneficial effects that speculators have on the commodity markets. As a consequence, the Commission takes into consideration the risk of deterring appropriate speculation when setting the federal limits. The Commission also preliminarily considered the exchange-suggested spot-month limits when setting the federal spot-month limit. As discussed below, in most cases the exchange-suggested limit levels reproposed by the Commission are the federal spot-month limit. Therefore, the Commission preliminarily believes that the federal limits are in line with the exchanges' expectations and therefore the exchanges would be unlikely, at least initially, to adopt a smaller exchange-set spot-month limit for the core referenced futures contracts. The Commission will also review the federal limits in the future to determine if they are effective and not unduly restrictive.

c. § 150.2(b) Single-Month and All-Months-Combined Speculative Position Limits

i. Summary of Changes

Reproposed § 150.2(b) provides that no person may hold or control positions, net long or net short, in referenced contracts in a single-month or in all-months-combined in excess of the levels specified by the Commission. In that regard, § 150.2(b) would require netting all positions in referenced contracts (regardless of whether such referenced contracts are physical-delivery or cash-settled) when calculating a person's positions for purposes of the proposed single-month or all-months-combined position limits (collectively ''non-spot-month'' position limits).[1274]

ii. Baseline

The baseline is the current § 150.2 of the Commission's regulations.

iii. Benefits and Costs

CEA section 4a(a)(3)(A) directs the Commission, each time it establishes limits, to set limits on speculative positions for months other than the spot-month.[1275] While market disruptions arising from the concentration of positions remain a possibility outside the spot month, the above-mentioned concerns about corners and squeezes and other forms of manipulation are reduced outside the spot-month. Accordingly, the Reproposal requires netting of physical-delivery and cash-settled referenced contracts for purposes of determining compliance with non-spot-month limits. The Commission has preliminarily determined it is appropriate to permit the additional flexibility in complying with the non-spot-months limits that netting allows, given the decreased risk of corners and squeezes outside the spot-month. Because this additional flexibility means market participants are able to retain offsetting positions outside of the spot-month, liquidity should not be significantly impaired and disruptions to price discovery should be reduced.

However, more generally, the Commission recognizes that federal non-spot month position limits do impose costs to exchanges and market participants. These costs are generally the same as discussed above with respect to § 150.2(a). The consideration of the costs to exchanges and market participants of § 150.2(a) is also applicable to § 150.2(b).

iv. Summary of Comments

Comments on this section are addressed in the discussion of 150.2(e) below.

d. § 150.2(c) Purpose of This Part

i. Summary of Changes

Reproposed § 150.2(c)(1) and (2) specify that for purposes of part 150, the spot month and any single month shall be those of the core referenced futures contract and that an eligible affiliate is not required to comply separately with speculative position limits.

ii. Baseline

The baseline is the current § 150.2 of the Commission's regulations.

iii. Benefits and Costs

The Commission believes these are conforming amendments to effectuate the rule and do not have cost or benefit implications.

[1271] *See* CL–MFA–60385 at 4. Citing testimony of Erik Haas (Director of Market Regulation, ICE Futures U.S.) at the EEMAC public meeting on February 26, 2105, the commenter asserted that the volume of over-the-counter transactions is already increasing because futures contracts have become too costly the further out the curve one goes. *Id.*

[1272] *See* CL–ISDA/SIFMA–59611 at Annex B at 5. This commenter referenced, but did not include, two papers as follows. James Hamilton and Jing Wu, Risk Premia in Crude Oil Futures Prices, NBER Working Paper (2013). Peter Christoffersen, Kris Jacobs, and Bingxin Li, Dynamic Jump Intensities and Risk Premiums in Crude Oil Futures and Options Markets, working paper (2013).

[1273] CL–Working Group–60947 at 14.

[1274] The Commission is reproposing to adopt the same level for single-month and all-months-combined limits, and refers to those limits as the ''non-spot-month limits.'' The spot month and any single month refer to those periods of the core referenced futures contract.

[1275] 7 U.S.C. 6a(a)(3)(A).

iv. Summary of Comments

No commenter addressed any cost or benefit considerations relating to proposed rules § 150.2(c)(1) or (2).

e. § 150.2(d) Core Referenced Futures Contracts

i. Summary of Changes

As defined in proposed § 150.1, referenced contracts are futures, options, or swaps contracts that are directly or indirectly linked to a core referenced futures contract or the commodity underlying a core referenced futures contract.[1276]

New rule § 150.2(d) lists the 25 core referenced futures contracts on which the Commission has preliminarily determined to establish federal speculative position limits. The list reflects a significant expansion of federal speculative position limits from the list of nine agricultural contracts under current part 150.[1277] The Commission has selected these important food, energy, and metals contracts on the basis that such contracts (i) have high levels of open interest and significant notional value and/or (ii) serve as a reference price for a significant number of cash market transactions. Thus, the Commission is reproposing position limits on these contracts in order to commence the expansion of its federal position limit regime with those commodity derivative contracts that it believes have the greatest impact on interstate commerce. The Commission will be reviewing other contracts going forward.

As discussed in the 2013 Position Limit Proposal,[1278] the Commission calculated the notional value of open interest (delta-adjusted) and open interest (delta-adjusted) for all futures, futures options, and significant price discovery contracts as of December 31, 2012 in all agricultural and exempt commodities as part of its selection of the 25 core referenced futures contracts in § 150.2(d). The Commission selected commodities in which the derivative contracts had largest notional value of open interest and open interest for three categories: Agricultural, energy, and metals. The Commission then designated the benchmark futures contracts for each commodity as the core referenced futures contract for which position limits would be established. Reproposed § 150.2(d) lists 16 core referenced futures contracts for agricultural commodities, four core referenced futures contracts for energy commodities, and five core referenced futures contracts for metals commodities.[1279]

ii. Baseline

The baseline is the current § 150.2 of the Commission's regulations.

iii. Benefits and Costs

The benefits and costs are considered in the discussion of the definition of core referenced futures contract and referenced contract in § 150.1.

iv. Summary of Comments

Comments on this section are considered in the discussion of the definition of core referenced futures contract and referenced contract in § 150.1.

f. § 150.2(e) Levels of Speculative Position Limits

i. Summary of Changes

The list of initial spot month, single month and all-months combined position limit levels adopted by the Commission for referenced contracts can be found in Appendix D to this part. Under reproposed § 150.2(e)(3), the Commission will recalibrate spot month position limit levels no less frequently than every two calendar years, with any such recalibration to result in limits no greater than one-quarter (25 percent) of the estimated spot-month deliverable supply[1280] in the relevant core referenced futures contract. This formula is consistent with the acceptable practices in current § 150.5, as well as the Commission's longstanding practice of using this measure of deliverable supply to evaluate whether DCM-set spot-month limits are in compliance with DCM core principles 3 and 5. The Reproposal separately restricts the size of positions in cash-settled referenced contracts that would potentially benefit from a trader's potential distortion of the price of the underlying core referenced futures contract.

Accordingly, each DCM is required to supply the Commission with an estimated spot-month deliverable supply figure that the Commission will use to recalibrate spot-month position limits unless the Commission decides to rely on its own estimate of deliverable supply instead.[1281]

In contrast to spot-month limits, which will be set as a function of deliverable supply, the formula for the non-spot-month position limits is based on total open interest for all referenced contracts that are aggregated with a particular core referenced futures contract. In that regard, § 150.2(e)(4) explains that the Commission will calculate non-spot-month position limit levels based on the following formula: 10 percent of the largest annual average open interest for the first 25,000 contracts and 2.5 percent of the open interest thereafter.[1282] As is the case with spot month limits, the Commission will adjust single month and all-months-combined limits no less frequently than every two calendar years.

The Commission's average open interest calculation will be computed for each of the past two calendar years, using either month-end open contracts or open contracts for each business day in the time period, as practical and in the Commission's discretion. Initially, the Commission is reproposing initial non-spot-month limits using the larger open interest level from two 12-month periods (July 1, 2104 to June 30, 2015; and July 1, 2015 to June 30, 2016), for futures contracts and options thereon reported under part 16, and for swaps reported under part 20.

In the future, the Commission expects to use the data reported pursuant to parts 16, 20, and/or 45 of the Commission's regulations to estimate average open interest in referenced contracts.[1283]

[1276] As discussed *above*, the definition of referenced contract excludes any guarantee of a swap, location basis contracts, commodity index contracts and trade option that meets the requirements of § 32.3 of this chapter.

[1277] 17 CFR 150.2.

[1278] December 2013 Position Limits Proposal, 78 FR 75725.

[1279] The Commission originally proposed in its 2013 to set position limits on 28 core referenced contracts, including the 25 contracts noted above plus CME Feeder Cattle, Lean Hog and Class III Milk. Those three contracts will not be included in the Reproposal for the reasons discussed above.

[1280] The guidance for meeting DCM core principle 3 (as listed in 17 CFR part 38 app. C) specifies that, ''[t]he specified terms and conditions [of a futures contract], considered as a whole, should result in a 'deliverable supply' that is sufficient to ensure that the contract is not susceptible to price manipulation or distortion. In general, the term 'deliverable supply' means the quantity of the commodity meeting the contract's delivery specifications that reasonably can be expected to be readily available to short traders and salable by long traders at its market value in normal cash marketing channels . . .'' *See* Core Principles and Other Requirements for Designated Contract Markets, 77 FR 36612, 36722 (Jun. 19, 2012).

[1281] § 150.2(e)(3)(ii)(A) would require DCMs to submit estimates of deliverable supply. DCM estimates of deliverable supplies (and the supporting data and analysis) would continue to be subject to Commission review. § 150.2(e)(3)(ii)(A) would allow a DCM to petition the Commission no less than two calendar months before the due date for submission of an estimate of deliverable supply to recommend that the Commission not change the spot-month limit.

[1282] Since 1999, the same 10 percent/2.5 percent methodology, now incorporated in current § 150.5(c)(2), has been used to determine futures all-months position limits for referenced contracts.

[1283] Options listed on DCMs would be adjusted using an option delta reported to the Commission pursuant to 17 CFR part 16; swaps would be

ii. Baseline

The baseline is the current § 150.2 of the Commission's regulations.

iii. Benefits and Costs

Method for Setting Spot-Month Position Limit Levels

The method for determining the levels at which the limits are set is consistent with the Commission's longstanding acceptable practices for DCM-set speculative position limits. In the December 2013 Position Limits Proposal, the Commission proposed to set the initial spot month speculative position limit levels for referenced contracts at the existing DCM-set levels for the core referenced futures contracts.[1284] As an alternative, the Commission stated that it was considering using 25 percent of an exchange's estimate of deliverable supply if the Commission verified the estimate as reasonable.[1285] As a further alternative, the Commission stated that it was considering setting initial spot month position limit levels at a recommended level, if any, submitted by a DCM (if lower than 25 percent of estimated deliverable supply).[1286]

In preliminarily determining the levels at which to set the initial speculative position limits, the Commission considered, among other things, the recommendations of the exchanges as well as data to which the exchanges do not have access. In considering these and other factors, a significant concern of the Commission became the effect of alternative limit levels on traders in the cash-settled referenced contracts. A DCM has reasonable discretion in establishing the manner in which it complies with core principle 5 regarding position limits.[1287] As the Commission observed in the December 2013 Position Limits Proposal, ''there may be a range of spot month limits, including limits set below 25 percent of deliverable supply, which may serve as practicable to maximize . . . [the] policy objectives [set forth in section 4a(a)(3)(B) of the CEA].'' [1288] The Commission must also consider the competitiveness of futures markets.[1289] Thus, the Commission preliminarily determined to accept the recommendations of the exchanges to set federal limits below 25 percent of deliverable supply, where setting a limit level at less than 25 percent of deliverable supply did not appear to restrict unduly positions in the cash-settled referenced contracts. The exchanges retain the ability to adopt lower exchange-set limit levels than the initial speculative position limit levels set by the Commission in this rulemaking.

As discussed in more detail above, the process of determining appropriate spot-month limit levels included the Commission receiving updated estimates of deliverable supply from the DCMs listing the 25 core referenced contracts, which Commission staff verified as reasonable after conducting its own independent review of estimated deliverable supply for the subject core referenced contracts. Furthermore, the DCMs provided recommended spot-month limit levels for some of the 25 core referenced contracts which the Commission considered while determining the appropriate level of spot-month limits for the 25 core referenced futures contracts.[1290] In addition, the Commission then conducted an impact analysis of different spot-month limit levels to discern how many market participants would be affected by the different limit levels.

As part of reproposing § 150.2(e)(3)(i), the Commission has considered scenarios where exchanges may or may not update deliverable supply. This may result in the Commission reviewing and re-establishing position limits in the spot month. Exchanges may elect not to undertake this expense of re-estimating the deliverable supply of the underlying

counted on a futures equivalent basis, equal to the economically equivalent amount of core referenced futures contracts reported pursuant to 17 CFR part 20 or as calculated by the Commission using swap data collected pursuant to 17 CFR part 45.

[1284] December 2013 Position Limit Proposal, 78 FR 75727. One commenter urged the Commission to retain the legacy speculative limits for enumerated agricultural products. The ''enumerated'' agricultural products refer to the list of commodities contained in the definition of ''commodity'' in CEA section 1a; 7 U.S.C. 1a. This list of agricultural contracts includes nine currently traded contracts: Corn (and Mini-Corn), Oats, Soybeans (and Mini-Soybeans), Wheat (and Mini-wheat), Soybean Oil, Soybean Meal, Hard Red Spring Wheat, Hard Winter Wheat, and Cotton No. 2. *See* 17 CFR 150.2. The position limits on these agricultural contracts are referred to as ''legacy'' limits because these contracts on agricultural commodities have been subject to federal positions limits for decades. This commenter stated, ''There is no appreciable support within our industry or, as far as we know, from the relevant exchanges to move beyond current levels. . . . Changing current limits, as proposed in the rule, will have a negative impact on futures-cash market convergence and will compromise contract performance.'' CL–American Farm Bureau Federation–59730 at 3). *Contra* CL–ISDA and SIFMA–59611 at 32 (setting initial spot-month limits at the existing exchange-set levels would be arbitrary because the exchange-set levels have not been calibrated to apply as ''a ceiling on the spot-month positions that a trader can hold across *all* exchanges for futures, options and swaps''); CL–ICE–59966 at 6 (''the Proposed Rule . . . effectively halves the present position limit in the spot month by aggregating across trading venues and uncleared OTC swaps''). *See also* CL–ISDA and SIFMA–59611 at 3 (the spot month limit methodology is ''both arbitrary and unjustified'').

[1285] December 2013 Position Limit Proposal, 78 FR 75727. The Commission also stated that if the Commission could not verify an exchange's estimate of deliverable supply for any commodity as reasonable, the Commission might adopt the existing DCM-set level or a higher level based on the Commission's own estimate, but not greater than would result from the exchange's estimated deliverable supply for a commodity.

One commenter was unconvinced that estimated deliverable supply is ''the appropriate metric for determining spot month position limits'' and opined that the ''real test'' should be whether limits ''allow convergence of cash and futures so that futures markets can still perform their price discovery and risk management functions.'' CL–NGFA–60941 at 2. Another commenter stated, ''While 25% may be a reasonable threshold, it is based on historical practice rather than contemporary analysis, and it should only be used as a guideline, rather than formally adopted as a hard rule. Deliverable supply is subject to numerous environmental and economic factors, and is inherently not susceptible to formulaic calculation on a yearly basis.'' CL–MGEX–60301 at 1. Another commenter expressed the view that the 25 percent formula is not ''appropriately calibrated to achieve the statutory objective'' set forth in section 4a(a)(3)(B)(i) of the CEA, 7 U.S.C. 6a(a)(3)(B)(i). CL–CME–60926 at 3. Another commenter opined that because the Commission ''has not established a relationship between 'estimated deliverable supply' and spot-month potential for manipulation or excessive speculation,'' the 25 percent formula is arbitrary. CL–ISDA and SIFMA–59611 at 31.

Several commenters opined that a limit at 25 percent of deliverable supply is too high. *E.g.,* CL–Americans for Financial Reform–59685 at 2; CL–Tri–State Coalition for Responsible Investment–59682 at 1; CL–CMOC–59720 at 3; CL–WEED–59628 (''Only a lower limit would ensure market stability and prevent market manipulation.''); CL-Public Citizen-60313 at 1 (''There is no good reason for a single firm to take 25% of a market.''); CL–IECA–59964 at 3 (25 percent of deliverable supply ''is a lot of market power in the hands of speculators''). One commenter stated that ''position limits should be set low enough to restore a commercial hedger majority in open interest in each core referenced contract,'' CL–Institute for Agriculture and Trade Policy (''IATP'')–60323 at 5, suggesting in a later submission that position limits at 5–10 percent of estimated deliverable supply in each covered contract applied on an aggregated basis might ''enable commercial hedgers to regain for all covered contracts their pre-2000 average share of 70 percent of agricultural contracts,'' CL–IATP–60394 at 2. One commenter supported expanding position limits ''to ensure rough or approximate convergence of futures and underlying cash at expiration.'' CL–Pamela D. Thornton (''Thornton'')–59702 at 1.

Several commenters supported setting limits based on updated estimates of deliverable supply which reflect current market conditions. *E.g.,* CL–ICE–59966 at 5; CL–FIA–59595 at 8; CL–EEI–EPSA–59602 at 9; CL–MFA–59606 at 5; CL–CMC–59634 at 14; CL–Olam–59658 at 3; CL–CCMC–59684 at 6–7.

[1286] December 2013 Position Limits Proposal, 78 FR at 75728.

[1287] CEA section 5(d)(1)(B), 7 U.S.C. 7(d)(1)(B).

[1288] December 2013 Position Limits Proposal, 78 FR at 75729.

[1289] CEA section 15(a)(2)(B), 7 U.S.C. 19(a)(2)(B).

[1290] The Commission notes that the CME did not provide a recommended spot month limit for its Live Cattle Contract. The Commission ultimately kept the current spot month limit of 450 contracts in place for the Live Cattle contract.

commodity. Among many reasons, this might be because the deliverable supply has not changed much during the time that the last estimate was made. In these cases, the Commission has the option to maintain the current spot month position limit level or use the formula based on the outdated deliverable supply estimate if different, or use the exchange's recommendation for the level of the spot month position limit. Sparing the exchanges of the cost of re-estimating the deliverable supply may be beneficial if the estimation costs are high or if the anticipated difference in the estimates is small. The Commission must also be mindful that exchanges might want the federal position limit to be set lower, because a lower limit might prevent liquidity in the exchange's core reference contract from developing on another exchange. Exchanges may elect to re-estimate deliverable supply. This would allow the Commission to maintain the current spot month level, replace it with the formula based on 25% of updated deliverable supply, or accept the exchange's recommendation for a different level. It is prudent to revise the spot month position limit if the deliverable supply has changed appreciably, because setting the limit too low might harm liquidity or setting it too high might make it easier for someone to engage in market manipulation such as perfecting a corner and squeeze.

iv. Summary of Comments

One commenter cautioned the Commission not to rely on inaccurate or unreliable data or apply a one-size-fits-all approach in setting the levels of position limits, in order to avoid potential harms to market liquidity and increased costs.[1291] Another commenter suggested that, in light of the complexities and costs of implementing federal and exchange-set limits, the Commission should not implement final rules until at least nine months after the final rule is issued.[1292]

The Commission has preliminarily determined to ease the transition to the initial speculative position limits by setting a compliance date of January 3, 2018 in § 150.3(e)(1). As for the process of determining appropriate spot-month position limit levels, the Commission endeavored to use accurate and reliable data. For example, the Commission looked to updated estimates of deliverable supply from the DCMs listing the 25 core referenced contracts, which Commission staff verified as reasonable after conducting its own independent review of estimated deliverable supply for the subject core referenced futures contracts.[1293] In addition, the Commission then conducted an impact analysis of different spot-month limit levels to discern how many market participants would be affected by the different limit levels. To determine the non-spot month position limits, the Commission used futures daily open interest data. In addition, it worked with market participants to improve the swap data collected pursuant to part 20 of the Commission's regulations, so that data could be used in determining open interest levels in the swap markets for referenced contracts. The Commission deems both the estimated deliverable supply data and exchange recommended spot-month limits along with the open interest data to be current and reliable for basing federal spot month and non-spot month limits, respectively.

g. Initial Speculative Spot Month Position Limit Levels

i. CME and MGEX Agricultural Contracts

For the CME and MGEX Agricultural (Legacy) contracts, which were previously subject to federal position limits, the Commission has preliminarily determined to set the initial speculative spot month position limit levels for C, O, RR, S, SM, SO, W and KW at the recommended levels submitted by CME,[1294] all of which are lower than 25 percent of estimated deliverable supply.[1295] As is evident from the table set forth in the discussion above, this also means that the Commission is reproposing the initial speculative position limit levels for these eight contracts as proposed. These initial levels track the existing DCM-set levels for the core referenced futures contracts;[1296] therefore, as noted in the December 2013 Position Limits Proposal, many market participants are already used to these levels and conform their practices accordingly.[1297] The Commission continues to believe this approach is consistent with the regulatory objectives of the Dodd-Frank Act amendments to the CEA.

The Commission has also preliminarily determined to set the initial speculative spot month position limit level for MWE at 1,000 contracts, which is the level requested by MGEX[1298] and approximately equal to 25 percent of estimated deliverable supply. This is an increase from the proposed level of 600 contracts and is greater than the initial speculative spot month position limit levels for W and KW.[1299] As stated in the December 2013 Position Limits Proposal, the 25 percent formula is consistent with the longstanding acceptable practices for DCM core principle 5.[1300] The Commission continues to believe, based on its experience and expertise, that the 25 percent formula is a reasonable "prophylactic tool to reduce the threat of corners and squeezes, and promote convergence without compromising market liquidity."[1301]

The Commission's impact analysis reveals no traders in cash settled contracts in any of C, O, S, SM, SO, W, MWE, KW, or RR, and no traders in physical delivery contracts for O and RR, above the initial speculative limit levels for those contracts. The Commission found varying numbers of traders in the C, S, SM, SO, W, MWE, KW physical delivery contracts over the initial levels, but the numbers were very small for MWE and KW. Because the levels that the Commission is adopting for C, O, S, SM, SO, W, KW, and RR maintain the status quo for those contracts, the Commission assumes that some or possibly all of such traders over the initial levels are hedgers. Hedgers may have to file for an applicable exemption, but hedgers with bona fide hedging positions should not have to reduce their positions as a result of speculative position limits per se. Thus, the number of traders in the C, S, SM, SO, W and KW physical delivery contracts who would need to reduce speculative positions below the initial limit levels should be lower than the numbers indicated by the impact

[1291] CL–Chamber–59684 at 4 and 5–6.

[1292] CL–FIA at 6 and 44.

[1293] The Commission notes that the CME did not provide a recommended spot month limit for its Live Cattle Contract. The Commission ultimately kept the current spot month limit of 450 contracts in place for the Live Cattle contract.

[1294] CL–CME–61007 at 5.

[1295] The Commission noted in the December 2013 Position Limits Proposal "that DCMs historically have set or maintained exchange spot month limits at levels below 25 percent of deliverable supply." December 2013 Position Limits Proposal, 78 FR 75729.

[1296] *See* CL–CME–61007 (specifying lower exchange-set limit levels for W and RR in certain circumstances).

[1297] December 2013 Position Limit Proposal, 78 FR 75727.

[1298] CL–MGEX–60938 at 2.

[1299] Most commenters who supported establishing the same level of speculative limits for each of the three wheat core referenced futures contracts focused on parity in the non-spot months. However, some commenters did support wheat party in the spot month, *e.g.,* CL–CMC–59634 at 15; CL–NCFC–59942 at 6.

[1300] December 2013 Position Limits Proposal, 78 FR 75729.

[1301] *Id.*

analysis. And, while setting initial speculative levels at 25 percent of deliverable supply would, based upon logic and the Commission's impact analysis, affect fewer traders in the C, S, SM, SO, W and KW physical delivery contracts, consistent with its statement in the December 2013 Position Limits Proposal, the Commission believes that setting these lower levels of initial spot month limits will serve the objectives of preventing excessive speculation, manipulation, squeezes and corners,[1302] while ensuring sufficient (in the view of the listing DCM) market liquidity for bona fide hedgers and ensuring that the price discovery function of the market is not disrupted.[1303]

Summary of Comments

MGEX contended that the proposed wheat position limit disparity (particularly in non-spot months) may inject significant instability into the market, as market participants will be unable to utilize time-tested risk management practices equally across the three contracts and have unintended negative market consequences resulting from hedgers and speculators limiting their activity (particularly spread trading) in markets with the lowest limits—or ceasing to trade in the lower-limit markets altogether.[1304]

MGEX was concerned that the proposed method inhibits growth in rapidly changing and expanding derivatives markets and will limit growth in the HRSW contract at a time when participation is increasing.[1305] MGEX asserted that the Proposed Rule has a disproportionate impact on HRSW market participants, given that MGEX HRSW has more large traders approaching the single month and all months combined limits than CBOT Wheat and KCBT Hard Winter Wheat despite the fact that the number of large traders approaching the Proposed Rule single month and all months combined limit levels stayed relatively constant among the three U.S. wheat contracts; MGEX also contended that price volatility or concentration in one contract may unduly affect the price of the others.[1306]

The Commission took concerns about wheat contract parity into account when preliminarily setting the spot month and non-spot month levels for the CBOT Wheat, KCBT Hard Winter Wheat and MGEX Hard Red Spring Wheat contracts. In that regard, as discussed below, the Commission is reproposing to maintaining the status quo for the non-spot month position limit levels for the KW and MWE core referenced futures contracts so that there will be partial wheat parity.[1307] The Commission has preliminarily determined not to raise the limit levels for KW and MWE to the limit level for W, as 32,800 contracts appears to be extraordinarily large in comparison to open interest in the KW and MWE markets, and the limit level for KW and MWE is already larger than a limit level based on the ''10, 2.5 percent'' formula. Even when relying on a single criterion, such as percentage of open interest, the Commission has historically recognized that there can ''result . . . a range of acceptable position limit levels.'' [1308]

ii. Softs

For the ''Softs''—agricultural contracts on cocoa, coffee, cotton, orange juice, sugar and live cattle—the Commission has preliminarily determined to set the initial speculative spot month position limit levels for the CC, KC, CT, OJ, SB, and SF [1309] core referenced futures contracts, based on the estimates of deliverable supply submitted by ICE,[1310] at 25 percent of estimated deliverable supply.[1311] As is evident from the table set forth in the discussion above, this also means that the Commission is reproposing initial speculative position limit levels that are significantly higher than the levels for these six contracts as proposed. As stated in the December 2013 Position Limits Proposal, the 25 percent formula is consistent with the longstanding acceptable practices for DCM core principle 5.[1312] The Commission continues to believe, based on its experience and expertise, that the 25 percent formula is a reasonable ''prophylactic tool to reduce the threat of corners and squeezes, and promote convergence without compromising market liquidity.'' [1313]

The Commission did not receive any estimate of deliverable supply for the CME (LC) core referenced futures contract from CME, nor did CME recommend any change in the limit level for LC. In the absence of any such update, the Commission is reproposing the initial speculative position limit level of 450 contracts as proposed. Of 616 reportable persons, the Commission's impact analysis did not reveal any unique person trading cash settled or physical delivery spot month contracts who would have held positions above this level for LC.

With respect to the IFUS CC, KC, CT, OJ, SB, and SF core referenced futures contracts, the Commission's impact analysis did not reveal any unique person trading cash settled spot month contracts who would have held positions above the initial levels that the Commission is adopting; as illustrated above. Rather, adopting lower levels would mostly have affected small numbers of traders in physical delivery contracts. Therefore, the Commission has preliminarily determined to accept ICE's recommendations.

iii. Metals

For the metals contracts, the Commission has preliminarily determined to set the initial speculative spot month position limit levels for GC, SI, and HG at the recommended levels submitted by CME,[1314] all of which are lower than 25 percent of estimated deliverable supply.[1315] In the case of GC and SI, this is a doubling of the current exchange-set limit levels.[1316] In the case

[1302] *Contra* CL–ISDA and SIFMA–59611 at 55 (proposed spot month limits ''are almost certainly far smaller than necessary to prevent corners or squeezes'').

[1303] December 2013 Position Limits Proposal, 78 FR 75729, Dec. 12, 2013.

[1304] CL–MGEX–59932 at 2.

[1305] CL–MGEX–60380 at 5.

[1306] CL–MGEX–59932 at 2. MGEX asserted that ''[w]ithout wheat contract parity—proven historically effective and efficient—inequities would be introduced into the marketplace that could well result in artificial market disruption through a lack of convergence, distorting the market and bringing no value to the price discovery process.'' Id.

[1307] Several commenters supported adopting equivalent non-spot month position limits for the three existing wheat referenced contracts traders. *E.g.,* CL–FIA–59595 at 4, 15; CL–CMC–60391 at 8; CL–CMC–60950 at 11; CL–CME–59718 at 44; CL–American Farm Bureau–59730 at 4; CL–MGEX–59932 at 2; CL–MGEX–60301 at 1; CL–MGEX–59610 at 2–3; CL–MGEX–60936 at 2–3; CL–NCFC–59942 at 6; CL–NGFA–59956 at 3.

[1308] Revision of Speculative Position Limits, 57 FR 12766, 12770 (Apr. 13, 1992). *See also* Revision of Speculative Position Limits and Associated Rules, 63 FR 38525, 38527 (July 17, 1998). *Cf.* December 2013 Position Limits Proposal, 78 FR 75729, Dec. 12, 2013 (there may be range of spot month limits that maximize policy objectives).

[1309] One commenter supported considering ''tropicals (sugar/coffee/cocoa) . . . separately from those agricultural crops produced in the US domestic market.'' CL–Thornton–59702 at 1; *see also* CL–Armajaro Asset Management–59729 at 1.

[1310] CL–CME–61007 at 5.

[1311] The Commission noted in the December 2013 Position Limits Proposal ''that DCMs historically have set or maintained exchange spot month limits at levels below 25 percent of deliverable supply.'' December 2013 Position Limits Proposal, 78 FR 75729, Dec. 12, 2013.

[1312] *Id.*

[1313] *Id.*

[1314] CL–CME–61007 at 5.

[1315] The Commission noted in the December 2013 Position Limits Proposal ''that DCMs historically have set or maintained exchange spot month limits at levels below 25 percent of deliverable supply.'' December 2013 Position Limits Proposal, 78 FR 75729, Dec. 12, 2013.

[1316] One commenter cautioned against raising limit levels for GC to 25 percent of deliverable supply, and expressed concern that higher federal

Continued

of HG, the initial level is the same as the existing DCM-set level for the core referenced futures contract, and lower than the level proposed. The Commission has also preliminarily determined to set the initial speculative spot month position limit level for PL at 100 contracts and PA at 500 contracts, which are the levels recommended by CME. In the case of PL and PA, the initial level is the same as the existing DCM-set level for the core referenced futures contract, and a decrease from the proposed levels of 500 and 650 contracts, respectively.

The Commission found varying numbers of traders in the GC, SI, PL, PA, and HG physical delivery contracts over the initial levels, but the numbers were very small except for PA. Because the levels that the Commission is adopting for PL, PA, and HG maintain the status quo for those contracts, the Commission assumes that some or possibly all of such traders over the initial levels are hedgers. The Commission reiterates the discussion above regarding agricultural contracts: hedgers may have to file for an applicable exemption, but hedgers with bona fide hedging positions should not have to reduce their positions as a result of speculative position limits per se. Thus, the number of traders in the metals physical delivery contracts who would need to reduce speculative positions below the initial limit levels should be lower than the numbers indicated by the impact analysis. And, while setting initial speculative levels at 25 percent of deliverable supply would, based upon logic and the Commission's impact analysis, affect fewer traders in the metals physical delivery contracts, consistent with its statement in the December 2013 Position Limits Proposal, the Commission believes that setting these lower levels of initial spot month limits will serve the objectives of preventing excessive speculation, manipulation, squeezes and corners,[1317] while ensuring sufficient market liquidity for bona fide hedgers in the view of the listing DCM and ensuring that the price discovery function of the market is not disrupted.

The Commission's impact analysis reveals no unique persons in the SI and HG cash settled referenced contracts, and very few unique persons in the cash settled GC referenced contract, whose positions would have exceeded the initial limit levels for those contracts. Based on the Commission's impact analysis, preliminarily setting the initial federal spot month limit levels for PL and PA at the lower levels recommended by CME impact a few traders in PL and PA cash settled contracts.

The Commission has considered the numbers of unique persons that would have been impacted by each of the cash-settled and physical-delivery spot month limits in the PL and PA referenced contracts. The Commission notes those limits would have impacted more traders in the physical-delivery PA contract than in the cash-settled PA contract, while fewer traders would have been impacted in the physical-delivery PL contract than in the cash-settled PL contract, albeit in any event few traders would have been impacted.[1318] The Commission also considered the distribution of those cash-settled traders over time; as reflected in the open interest table discussed above regarding setting non-spot month limits, it can be readily observed that open interest in each of the cash-settled PL and PA referenced contracts was markedly lower in the second 12-month period (year 2) than in the prior 12-month period (year 1). Accordingly, the Commission preliminarily concludes that the CME recommended levels in PL and PA referenced contracts are acceptable.

iv. Energy

For the energy contracts, the Commission has preliminarily determined to set the initial speculative spot month position limit levels for the NG, CL, HO, and RB core referenced futures contracts at 25 percent of estimated deliverable supply which, in the case of CL, HO, and RB is higher than the levels recommended by CME.[1319] As is evident from the table set forth above, this also means that the Commission is adopting initial speculative position limit levels that are significantly higher than the proposed levels for these four contracts. As stated in the December 2013 Position Limits Proposal, the 25 percent formula is consistent with the longstanding acceptable practices for DCM core principle 5.[1320] The Commission continues to believe, based on its experience and expertise, that the 25 percent formula is a reasonable ''prophylactic tool to reduce the threat of corners and squeezes, and promote convergence without compromising market liquidity.''[1321]

The levels that CME recommended for NG, CL, HO, and RB are twice the existing exchange-set spot month limit levels. Nevertheless, the Commission is proposing to set the initial speculative spot month limit levels at 25 percent of deliverable supply for CL, HO, and RB because the higher levels will lessen the impact on a number of traders in both cash settled and physical delivery contracts. For NG, the Commission is proposing to set the physical delivery limit at 25 percent of deliverable supply, as recommended by CME; the Commission is also proposing to set a conditional spot month limit exemption of 10,000 for NG only.[1322] This exemption would to some degree maintain the status quo in natural gas because each of the NYMEX and ICE cash settled natural gas contracts, which settle to the final settlement price of the physical delivery contract, include a conditional spot month limit exemption of 5,000 contracts (for a total of 10,000 contracts).[1323] However, neither

limits would incentivize exchanges to raise their own limits. CL–WGC–59558 at 2–4.

[1317] *Contra* CL–ISDA and SIFMA–59611 at 55 (proposed spot month limits ''are almost certainly far smaller than necessary to prevent corners or squeezes'').

[1318] In this regard, the Commission notes that CME did not have access to the Commission's impact analysis when CME recommended levels for its physical-delivery core referenced futures contracts.

[1319] CL–CME–61007 at 5. One commenter opined that 25 percent of deliverable supply would result in a limit level that is too high for natural gas, and suggest 5 percent as an alternative that ''would provide ample liquidity and significantly reduce the potential for excessive speculation.'' CL–IECA–59964 at 3.

[1320] December 2013 Position Limits Proposal, 78 FR at 75729.

[1321] *Id.*

[1322] This exemption for up to 10,000 contracts would be five times the spot month limit of 2,000 contracts, consistent with the December 2013 Position Limits Proposal. *See* December 2013 Position Limits Proposal, 78 FR at 75736–8. Under vacated § 151.4, the Commission would have applied a spot-month position limit for cash-settled contracts in natural gas at a level of five times the level of the limit for the physical delivery core referenced futures contract. *See* Position Limits for Futures and Swaps, 76 FR 71626, 71687 (Nov. 18, 2011).

[1323] Some commenters supported retaining a conditional spot month limit in natural gas. *E.g.,* CL–ICE–60929 at 12 (''Any changes to the current terms of the Conditional Limit would disrupt present market practice for no apparent reason. Furthermore, changing the limits for cash-settled contracts would be a significant departure from current rules, which have wide support from the broader market as evidenced by multiple public comments supporting no or higher cash-settled limits.''). *Contra* CL–Levin–59637 at 7 (''The proposed higher limit for cash settled contracts is ill-advised. It would not only raise the affected position limits to levels where they would be effectively meaningless, it would also introduce market distortions favoring certain contracts and certain exchanges over others, and potentially disrupt important markets, including the U.S. natural gas market that is key to U.S. manufacturing.''); CL–Public Citizen–59648 at 5 (''Congress, in allowing an exemption for bona fide hedgers but not pure speculators, could not possibly have intended for the Commission to implement position limits that allow market speculators to hold 125 percent of the estimated deliverable supply. Once again, while this

NYMEX and ICE penultimate contracts, which settle to the daily settlement price on the next to last trading day of the physical delivery contract, nor OTC swaps, are currently subject to any spot month position limit. In addition, the Commission's impact analysis suggests that a conditional spot month limit exemption greater than 25 percent of deliverable supply for cash settled contracts in CL, HO, and RB would potentially benefit only a few traders, while a conditional spot month limit exemption for cash settled contracts in NG would potentially benefit many traders.

Summary of Comments

One economist estimated, using various stated assumptions but not an empirical model, that position limits at the proposed level would cost American consumers roughly $100 billion, based on an increase of $15 per barrel of oil in 2013.[1324] This economist also asserted that position limits (or the mere possibility that such limits may be tightened) would discourage passive investors from the commodity derivative sector and, thus, would adversely affect investment in the oil and gas industry by raising the cost of hedging for exploration firms.[1325] This economist believes that position limits would increase costs whether or not the position limits actually restrict a market participant's trading, because compliance costs such as recordkeeping and reporting would modestly increase the costs of drilling associated with the regulations and discourage market entry.[1326]

The Commission believes that positon limits are unlikely to deter passive investors because they have the opportunity to invest in commodities through collective investment vehicles such as exchange traded funds (ETFs) or commodity pools. For example, if a position limit would become binding on a particular ETF, market demand would be expected to encourage another party to create a new ETF that could replicate a similar strategy to the previous one, which would allow the passive investment to continue.

Regarding the forms and application process to obtain a § 150.11 exemption, the Commission believes that the requirements are not as onerous as the commenter fears. In this regard, an oil exploration firm would likely be able to qualify for an anticipatory hedge exemption. The Commission believes the costs of this process will have a negligible impact on the oil exploration firm's costs of hedging.

Another commenter was concerned that position limits set so low as to diminish speculative capacity in U.S. energy markets will distort prices, increase volatility, increase option premiums and increase the cost of hedging.[1327]

The Commission agrees with the commenter that setting position limits too low could distort prices, increase volatility, increase option premiums and increase the cost of hedging. The Commission believes it has preliminarily set the limit levels sufficiently high so that they will not have a significant adverse impact on the efficiency and price discovery functions of the core referenced futures contracts.

In response to 2016 Supplemental Position Limits Proposal RFC 55, a commenter pointed out that the Commission's Division of Enforcement has numerous tools at its disposal, and the exchanges have position step-down and exemption revocation authorization at their disposal, to enforce market manipulation prohibitions.[1328]

The Commission agrees with the commenter, but notes that the Division of Enforcement's tools can be used only after market manipulation or other adverse consequences have already occurred. As for the tools at the disposal of the exchanges to reduce a market participant's position or deter it from attempting to manipulate the market, the Commission considered these points when preliminarily setting the federal position limits at levels that may be higher than the Commission would otherwise consider, and in some cases higher than the levels suggested by the exchanges.

h. Method for Setting Single-Month and All-Months Combined Position Limit Levels

As discussed in more detail above, the Commission has preliminarily determined to use the futures position limits formula, 10 percent of the open interest for the first 25,000 contracts and 2.5 percent of the open interest thereafter (*i.e.,* the ''10, 2.5 percent'' formula), to set non-spot month speculative position limits for referenced contracts. This was the method proposed in the December 2013 Position Limits Proposal. The Commission used a combination of data on open interest in physical commodity futures and options from the relevant exchanges and adjusted part 20 swaps data covering a total of 24 months, rather than two calendar years of data in setting the initial non-spot month position limit levels.[1329] The Commission continues to believe that ''the non-spot month position limits would restrict the market power of a speculator that could otherwise be used to cause unwarranted price movements.'' [1330] In preliminarily determining the appropriate non-spot month limit levels the Commission considered the results of its impact analysis of different non-spot month limit levels to discern how many market participants would be affected by different limit levels.

In addition, the Commission believes that it is beneficial to update the non-spot month position limits based on recent position data, such as Part 20 data. The Commission also proposes to retain the option to maintain the existing position limit levels if it believes there is good reason to deviate from the formulas. This could be the case if, for example, the Commission has experience at a level higher the amount given in the formula and believes that the higher level is appropriate, because the Commission has not observed any problems at the higher level. Furthermore, the

exception for cash-settled contracts would avoid market manipulations such as corners and squeezes (since cash-settled contracts give no direct control over a commodity), it does not address the problem of undue speculative influence on futures prices.''). One commenter urged the Commission ''to eliminate the requirement that traders hold no physical-delivery position in order to qualify for the conditional spot-month limit exemption'' in order to maintain liquidity in the NYMEX natural gas futures contract. CL–BG–59656 at 6–7. *See also* CL–APGA at 8 (the Commission should condition the spot month limit exemption for cash settled natural gas contracts by precluding a trader from holding more than one quarter of the deliverable supply in physical inventory). *Cf.* CL–CME–59971 at 3 (eliminate the five times natural gas limit because it ''encourages participants to depart from, or refrain from establishing positions in, the primary physical delivery contract market and instead opt for the cash-settled derivative contract market, especially during the last three trading days when the five times limit applies. By encouraging departure from the primary contract market, the five times limit encourages a process of de-liquefying the benchmark physically delivered futures market and directly affects the determination of the final settlement price for the NYMEX NG contract- the very same price that a position representing five times the physical limit will settle against.'').

[1324] CL–ISDA/SIFMA–59611 at Annex A at 3. The economist noted that he used a ''methodology for predicting changes in crude oil prices linked to global inventory levels.'' *Id.*

[1325] *Id.* at 9.

[1326] *Id.* at 10.

[1327] CL–Vectra–60369 at 1–2. The commenter was particularly concerned that given the ''dearth of speculative capacity'' in many energy contracts, hedging costs would increase and be passed on to consumers. *Id.*

[1328] CL–IECAssn–60949 at 23.

[1329] Commission staff analyzed and evaluated the quality of part 20 data for the period from July 1, 2014 through June 30, 2015 (''Year 1''), and the period from July 1, 2015 through June 30, 2016 (''Year 2'').

[1330] December 2013 Position Limits Proposal, 78 FR 75730, Dec. 12, 2013.

Commission has preliminarily determined that it will fix subsequent levels no less frequently than every two calendar years. This conclusion is reproposed in § 150.2(e)(2).

i. CME and MGEX Agricultural Contracts

The Commission is reproposing non-spot month speculative position limit levels for the Corn (C), Oats (O), Rough Rice (RR), Soybeans (S), Soybean Meal (SM), Soybean Oil (SO), and Wheat (W) core referenced futures contracts based on the 10, 2.5 percent open interest formula.[1331] Based on the Commission's experience since 2011 with non-spot month speculative position limit levels for the Hard Red Winter Wheat (KW) and Hard Red Spring Wheat (MWE) core referenced futures contracts, the Commission is proposing to maintain the limit levels for those two commodities at the current level of 12,000 contracts rather than reducing them to the lower levels that would result from applying the 10, 2.5 percent formula.[1332]

Maintaining the status quo for the non-spot month limit levels for the KW and MWE core referenced futures contracts means there will be partial wheat parity.[1333] The Commission has preliminarily determined not to raise the limit levels for KW and MWE to the limit level for W, as 32,800 contracts appears to be extraordinarily large in comparison to open interest in the KW and MWE markets, and the limit level for KW and MWE is already larger than a limit level based on the 10, 2.5 percent formula. Even when relying on a single criterion, such as percentage of open interest, the Commission has historically recognized that there can ''result . . . a range of acceptable position limit levels.'' [1334]

ii. Softs

The Commission is reproposing non-spot month speculative position limit levels for the CC, KC, CT, OJ, SB, SF and LC [1335] core referenced futures contracts based on the 10, 2.5 percent open interest formula.

iii. Metals

The Commission is reproposing non-spot month speculative position limit levels for the GC, SI, PL, PA, and HG core referenced futures contracts based on the 10, 2.5 percent open interest formula.[1336]

iv. Energy

The Commission is reproposing non-spot month speculative position limit levels for the NG, CL, HO, and RB core referenced futures contracts based on the 10, 2.5 percent open interest formula.[1337]

Summary of Comments

A commenter claimed that the proposed rule did not address the price impact of speculative money flows into commodities, and that if the Commission is concerned with the types of manipulative activities shown by the Hunt Brothers and Amaranth cases, there are ''targeted and less burdensome and complex ways to prevent such a manipulative harm'' and the inclusion of position limits on swaps is invalid because swaps cannot be used to cause this detrimental impact.[1338]

The Commission disagrees, and notes that swaps can be used to cause detrimental impact, as occurred in the Amaranth case. Amaranth entered into swaps on an exempt commercial market that were directly linked to a core reference futures contract. So to ignore swaps would not adequately address the issue that position limits are intended to address.

i. § 150.2(f)–(g) Pre-Existing Positions and Positions on Foreign Boards of Trade

i. Summary of Changes

The Commission is reproposing new § 150.2(f)(2) to exempt from federal non-spot-month speculative position limits any referenced contract position acquired by a person in good faith prior to the effective date of such limit, provided that the pre-existing position is attributed to the person if such person's position is increased after the effective date of such limit.[1339]

Finally, reproposed § 150.2(g) will apply position limits to positions on FBOTs provided that positions are held in referenced contracts that settle to a referenced contract and the FBOT allows direct access to its trading system for participants located in the United States.

[1331] One commenter expressed concern ''that proposed all-months-combined speculative position limits based on open interest levels is not necessarily the appropriate methodology and could lead to contract performance problems.'' This commenter urged ''that all-months-combined limits be structured to 'telescope' smoothly down to legacy spot-month limits in order to ensure continued convergence.'' CL–National Grain and Feed Association–60312 at 4.

[1332] One commenter supported a higher limit for KW than proposed to promote growth and to enable liquidity for Kansas City hedgers who often use the Chicago market. CL–Citadel–59717 at 8. Another commenter supported setting ''a non-spot month and combined position limit of no less than 12,000 for all three wheat contracts.'' CL–MGEX–60301 at 1. *Contra* CL–Occupy the SEC–59972 at 7–8 (commending ''the somewhat more restrictive limitations . . . on wheat trading'').

[1333] Several commenters supported adopting equivalent non-spot month position limits for the three existing wheat referenced contracts traders. *See, e.g.,* CL–FIA–59595 at 4, 15; CL–CMC–60391 at 8; CL–CMC–60950 at 11; CL–CME–59718 at 44; CL–American Farm Bureau–59730 at 4; CL–MGEX–59932 at 2; CL–MGEX–60301 at 1; CL–MGEX–59610 at 2–3; CL–MGEX–60936 at 2–3; CL–NCFC–59942 at 6; CL–NGFA–59956 at 3.

[1334] Revision of Speculative Position Limits, 57 FR 12770, 12766, Apr. 13, 1992. *See also* Revision of Speculative Position Limits and Associated Rules, 63 FR 38525, 38527, Jul. 17, 1998. *Cf.* December 2013 Position Limits Proposal (there may be range of spot month limits that maximize policy objectives), 78 FR 75729, Dec. 12, 2013.

[1335] One commenter expressed concern that too high non-spot month limit levels could lead to a repeat of convergence problems experienced by certain contracts and that ''the imposition of all months combined limits in continuously produced non-storable commodities such as livestock . . . will reduce the liquidity needed by hedgers in deferred months who often manage their risk using strips comprised of multiple contract months.'' CL–American Farm Bureau Federation–59730 at 3–4. One commenter requested that the Commission withdraw its proposal regarding non-spot month limits, citing, among other things, the Commission's previous approval of exchange rules lifting all-months-combined limits for live cattle contracts ''to ensure necessary deferred month liquidity.'' CL–CME–59718 at 4. Another commenter expressed concern that non-spot month limits would have a negative impact on live cattle market liquidity. CL–''CMC'')–59634 at 12–13. *See also* CL–CME–59718 at 41.

[1336] One commenter was concerned that applying the 10, 2.5 percent formula to open interest for gold would result in a lower non-spot month limit level than the spot month limit level, and urged the Commission to ''apply a consistent methodology to both spot and non-spot months.'' CL–WGC–59558 at 5.

[1337] One commenter suggested deriving non-spot month limit levels for the CL, HO, and RB referenced contracts from the usage ratios for US crude oil and oil products rather than open interest and expressed concern that ''unnecessarily low limits will hamper legitimate hedging activity.'' CL–Citadel–59717 at 7–8. Another commenter suggested setting limit levels based on customary position size. CL–APGA–59722 at 6. This commenter also supported setting the single month limit at two-thirds of the all months combined limit in order to relieve market congestion as traders exit or roll out of the next to expire month into the spot month. CL–APGA–59722 at 7.

[1338] CL–COPE–59662 at 5. The commenter asserted that the Commission's position limits proposal was based solely on concerns about attempts to manipulate the price discovery contract or hoard physical inventory because the Commission highlighted only the Amaranth and Hunt Brothers cases. *Id.*

[1339] *See also* the definition of the term ''Pre-existing position'' adopted in § 150.1. Such pre-existing positions that are in excess of the position limits will not cause the trader to be in violation based solely on those positions. To the extent a trader's pre-existing positions would cause the trader to exceed the non-spot-month limit, the trader could not increase the directional position that caused the positions to exceed the limit until the trader reduces the positions to below the position limit. As such, persons who established a net position below the speculative limit prior to the enactment of a regulation would be permitted to acquire new positions, but the total size of the pre-existing and new positions may not exceed the applicable limit.

ii. Baseline

The baseline is the current § 150.2 of the Commission's regulations.

iii. Benefits and Costs

The Commission exempted certain pre-existing positions from position limits under new § 150.2(f) as part of its grandfathering provisions.[1340] Essentially, this means only futures contracts initially will be subject to non-spot month position limits, as well as swaps entered after the compliance date. The Commission notes that a pre-existing position in a futures contract also would not be a violation of a non-spot month limit, but, rather, would be grandfathered, as discussed under § 150.2(f)(2). Therefore, market participants can more easily adjust their existing positions to the new federal position limit regime. Market participants will however incur costs for newly established positions in the relevant swaps after the compliance date, such as those discussed above such as the costs of monitoring their positions with respect to any applicable federal position limit and applying for exemptions should they need to exceed those limits.

New § 150.2(g), extends the federal position limits to a person who holds positions in referenced contracts on an FBOT that settle against any price of one or more contracts listed for trading on a DCM or SEF that is a trading facility, if the FBOT makes available such referenced contracts to its members or other participants located in the United States through direct access to its electronic trading and ordering matching system. In that regard, § 150.2(g) is consistent with CEA section 4a(a)(6)(B), which directs the Commission to apply aggregate position limits to FBOT linked, direct-access contracts.[1341]

Regulations 150.2(f) and (g) implement statutory directives in CEA section 4a(b)(2) and CEA section 4a(a)(6)(B), respectively, and are not acts of the Commission's discretion. Thus, a consideration of costs and benefits of these provisions is not required under CEA section 15(a).

iv. Summary of Comments

No commenter addressed the costs or benefits of § 150.2(f) and (g).

[1340] The Commission excluded from position limits ''pre-enactment swaps'' and ''transition period swaps,'' in its grandfathering provisions, as discussed above.

[1341] *See supra* discussion of CEA section 4a(a)(6) concerning aggregate position limits and the treatment of FBOT contracts.

5. Section 150.3—Exemptions From Federal Position Limits

As discussed above, the Commission has provided a general discussion of reproposed § 150.3 and highlighted the rule-text changes that it has made after several rounds of proposed rulemakings and responsive comments. In this release, the Commission has reproposed paragraphs (a), (b), (d), (e), (g) and (h) as proposed in December 2013.[1342] The Commission has amended the text in proposed § 150.3(c) and (f). In the December 2013 proposal, the Commission also discussed the costs and benefits of these two paragraphs, as well as, paragraphs (a), (b), (d), (e), (g) and (h).[1343]

In the June 2016 Supplemental Position Limits Proposal, the Commission changed proposed paragraph (a). The Commission also explained in the 2016 cost-benefit section that the changes it was making to proposed § 150.3(a)(1) should be read in conjunction with proposed §§ 150.9, 150.10, and 150.11.[1344] Between the June 2016 changes to §§ 150.9, 150.10, and 150.11 and now, the Commission has not made additional changes to § 150.3(a)(1). In general, the proposed changes made in the June 2016 Supplemental Position Limits Proposal detailed processes that exchanges could offer to market participants who seek exemptions for positions to exchange-set and federal position limits.

In this section, the Commission summarizes reproposed § 150.3, and, thereafter, discusses the related benefits and costs of the final rules.

a. Section 150.3 Rule Summaries

i. Section 150.3(a)—Bona Fide Hedging Exemption

Among other things, reproposed § 150.3(a)(1)(i) codifies the statutory requirement that bona fide hedging positions be exempt from federal position limits. Reproposed § 150.3(a)(2) authorizes other exemptions from position limits for financial-distress positions, conditional spot-month limit positions, spread positions, and other risk-reduction practices.

ii. Section 150.3(b)—Financial Distress Exemption

Reproposed § 150.3(b) provides the means for market participants to request relief from applicable position limits during certain financial distress circumstances, including the default of a customer, affiliate, or acquisition target of the requesting entity, that may require an entity to assume in short order the positions of another entity.

iii. Section 150.3(c)—Conditional Spot-Month Position Limit Exemption

Reproposed § 150.3(c) provides a conditional spot-month limit exemption that permits traders to acquire positions for natural gas up to 10,000 contracts if such positions are exclusively in cash-settled contracts. The natural-gas conditional exemption would not be available to traders who hold or control positions in the spot-month physical-delivery referenced contract in order to reduce the risk that traders with large positions in cash-settled contracts would attempt to distort the physical-delivery price to benefit such positions.

iv. Section 150.3(d)—Pre-Enactment and Transition Period Swaps Exemption

Reproposed § 150.3(d) provides an exemption from federal position limits for swaps entered into before July 21, 2010 (the date of the enactment of the Dodd-Frank Act), the terms of which have not expired as of that date, and for swaps entered into during the period commencing July 22, 2010, the terms of which have not expired as of that date, and ending 60 days after the publication of final rule § 150.3—that is, its effective date.

v. Section 150.3(e)—Other Exemptions

Reproposed § 150.3(e) explains that a market participant engaged in risk-reducing practices that are not enumerated in the revised definition of bona fide hedging in reproposed § 150.1 may use two different methods to apply to the Commission for relief from federal position limits. The market participant may request an interpretative letter from Commission staff pursuant to § 140.9 concerning the applicability of the bona fide hedging position exemption, or may seek exemptive relief from the Commission under CEA section 4a(a)(7) of the Act.

vi. Section 150.3(f)—Previously Granted Exemptions

After reviewing comments, the Commission has preliminarily determined it is best to change the § 150.3(f) text proposed in December 2013. The amended text broadens exemption relief to pre-existing financial instruments that are within current § 1.47's scope, and to exchange-granted non-enumerated exemptions in non-legacy commodity derivatives

[1342] December 2013 Proposal, 78 FR 75828, Dec. 12, 2013.

[1343] Reproposed § 150.3 has ten paragraphs: (a) through (j). Reproposed § 150.3(i) (aggregation of accounts) and (j) (delegation of authority to DMO Director) do not have cost-benefit implications, and are not discussed in this section.

[1344] For a fuller discussion of all the changes to reproposed § 150.3, *see* Section III.C., above.

outside of the spot month with other conditions.

vii. Section 150.3(g) and (h)—Recordkeeping

Reproposed § 150.3(g)(1) specifies recordkeeping requirements for market participants who claim any exemption in final § 150.3. Market participants claiming exemptions under reproposed § 150.3 would need to maintain complete books and records concerning all details of their related cash, forward, futures, options and swap positions and transactions. Reproposed § 150.3(g)(2) requires market participants seeking to rely upon the pass-through swap offset exemption to obtain a representation from its counterparty and keep that representation on file. Similarly, reproposed § 150.3(g)(3) requires a market participant who makes such a representation to maintain records supporting the representation. Under reproposed § 150.3(h), all market participants would need to make such books and records available to the Commission upon request, which would preserve the ''call for information'' rule set forth in current § 150.3(b).

b. Baseline

The baseline is the current § 150.3 of the Commission's regulations.

c. Benefits and Discussion of Comments

i. Section 150.3(a)—Positions Which May Exceed Limits

As explained in the December 2013 Supplemental Position Limits Proposal, § 150.3 works with §§ 150.9, 150.10, and § 150.11. All of these rules operate together within the broader position-limits regulatory regime and provide significant benefits, such as regulatory certainty, consistency, and transparency. As such, the benefits of reproposed § 150.3 are discussed in the cost-benefit sections related to reproposed §§ 150.9, 150.10, and 150.11.

ii. Section 150.3(b)—Financial Distress Exemption

The Commission continues to believe that by codifying historical practices of temporarily lifting position limit restrictions several benefits will ensue. Reproposed § 150.3 ensures the orderly transfers of positions from financially distressed firms to financially secure firms or facilitating other necessary remediation measures during times of market stress. Because of this Reproposal, the Commission believes it is less likely that positions will be prematurely or unnecessarily liquidated, and it is less likely that the price-discovery function of markets will be harmed.

iii. Section 150.3(c)—Conditional Spot Month Limit Exemption

In the December 2013 proposal, the Commission proposed § 150.3(c) that provided speculators with an opportunity to maintain relatively large positions in cash-settled contracts up to but no greater than 125 percent of the spot-month limit. The Commission explained that by prohibiting speculators using the exemption in the cash-settled contract from trading in the spot-month of the physical-delivery contract, the final rules should further protect the delivery and settlement process, and reduce the ability for a trader with a large cash settled contract position to attempt to manipulate the physical-delivery contract price in order to benefit his position. The Commission invited comment on this general exemption. Upon review of the comment letters, the Commission has preliminarily determined to restrict the conditional-spot-month-limit exemption to natural gas cash-settled referenced contracts. The reasons for this change are explained above.

iv. Section 150.3(d)—Pre-Enactment and Transition Period Swaps Exemption

The pre-existing swaps exemption in reproposed§ 150.3(d) is consistent with CEA section 4a(b)(2). The exemption promotes the smooth transition for previously unregulated swaps markets to swaps markets that will be subjected to position limits compliance. In addition, allowing netting with pre-enactment and transition swaps provides flexibility where possible in order to lessen the impact of the regime on entities with swap positions.

v. Section 150.3(e)—Other Exemptions

Reproposed § 150.3(e) is essentially clarifying and organizational in nature. For the most part, the Reproposal provides the benefit of regulatory certainty for those granted exemptions.

vi. Section 150.3(f)—Other Exemptions and Previously Granted Exemptions

As explained above, the Commission has expanded the scope of reproposed § 150.3(f) exemptive relief. In December 2013, the Commission discussed the benefits of proposed § 150.3(f), and believed that the benefits centered on regulatory certainty. Now that the Commission has increased the types of financial instruments that may be exempted from position limits under this rule, the Commission believes that it has reduced the likelihood of market disruption because of forced and unexpected liquidations. In other words, the Commission believes that reproposed § 150.3(f) will support market stability.

vii. Section 150.3(g) and (h)—Recordkeeping and Special Calls

The Commission believes that the reproposed § 150.3(g)'s recordkeeping requirements are critical to the Commission's ability to effectively monitor compliance with exemption eligibility standards. Because the Commission will have access to records under § 150.3(h), it will be able to assess whether exemptions are susceptible to abuse and to support the position-limits regime, which, among other things, aims to prevent excessive speculation and/or market manipulation.

d. Costs and Discussion of Comments

As the Commission expressed in the December 2013 Supplemental Position Limits Proposal, the exemptions under reproposed § 150.3 do not increase the costs of complying with position limits. The Commission continues to believe that many costs will likely decrease by the Commission providing for relief from position limits in certain situations. The reproposed § 150.3 exemptions are elective, so no entity is required to assert an exemption if it determines the costs of doing so do not justify the potential benefit resulting from the exemption. While the Commission appreciates that there will be compliance duties connected to the reproposed § 150.3, the Commission does not anticipate the costs of obtaining any of the exemptions to be overly burdensome.[1345]

i. Section 150.3(a)—Positions Which May Exceed Limits

Because of the proposed changes in the June 2016 Supplemental Position Limits Proposal, reproposed § 150.3(a) must be read with reproposed §§ 150.9, 150.10, and § 150.11. Moreover, the costs of reproposed § 150.3 are linked to reproposed §§ 150.9, 150.10, and § 150.11, and are discussed more fully below.

ii. Section 150.3(b)—Financial Distress Exemption

The Commission's view on the costs related to the financial distress exemption under reproposed § 150.3(b) remains unchanged. The costs are likely to be minimal. Market participants who voluntarily employ these exemptions will incur filing and recordkeeping

[1345] *See, e.g.,* the discussion of costs related to non-enumerated bona fide hedging position determinations, anticipatory bona fide hedge filings, and spread exemptions below.

costs. As explained in the 2013 proposal, the Commission cannot accurately estimate how often this exemption may be invoked because emergency or distressed market situations are unpredictable and dependent on a variety of firm- and market-specific factors as well as general macroeconomic indicators. The Commission, nevertheless, believes that emergency or distressed market situations that might trigger the need for this exemption will be infrequent. The Commission continues to assume that reproposed § 150.3(b) will add transparency to the process. Finally, the Commission believes that in the case that one firm is assuming the positions of a financially distressed firm, the costs of claiming the exemption would be incidental to the costs of assuming the position.

iii. Section 150.3(c)—Conditional Spot Month Limit Exemption

A natural gas market participant that elects to exercise this exemption will incur certain direct costs to do so. The natural gas market participant must file Form 504 in accordance with requirements listed in reproposed § 19.01. The Commission does not believe that there will be additional costs, or at least not significant costs, because exchanges already have the exemption. Given that there has been experience with this type of exemption for natural gas market participants,[1346] the Commission does not believe that liquidity, in the aggregate (across the core referenced futures contract and referenced contracts) will be adversely impacted.[1347] By retaining the exemption for natural gas contracts, the Commission has heeded commenters concerns about disrupting market practices and harming liquidity in the cash market, thus increasing the cost of hedging and possibly preventing convergence between the physical-delivery futures and cash markets.

iv. Section 150.3(d)—Pre-Enactment and Transition Period Swaps Exemption

The exemption offered in reproposed § 150.3(d) is self-executing and will not require a market participant to file for relief. Nevertheless, as explained in the December 2013 proposal, a market participant may incur costs to identify positions eligible for the exemption and to determine if that position is to be netted with post-enactment swaps for purposes of complying with a non-spot-month position limit. The Commission believes these costs will not be overly burdensome, and notes that market participants who assume such costs do so voluntarily.

v. Section 150.3(e)—Other Exemptions and Previously Granted Exemptions

Under the reproposed § 150.3(e), market participants electing to seek an exemption other than those specifically enumerated, will incur certain direct costs to do so. The Commission discussed the expected costs in the December 2013 proposal and continues to believe that the same costs will arise should market participants elect exemptive relief under reproposed § 150.3(e). As explained in the December 2013 proposal, market participants will incur costs related to petitioning the Commission under § 140.99 of the Commission's regulations or under CEA section 4a(a)(7). There also will be recordkeeping costs for those market participants who elect to pursue a § 150.3(e) exemption. The Commission believes that these costs will be minimal, as participants already maintain books and records under a variety of other Commission regulations and as the information required in these sections is likely already being maintained. The Commission has estimated the costs entities might incur and discussed those costs in the PRA section of this release.

vi. Section 150.3(f)—Previously Granted Exemptions

Market participants who had previously relied upon the exemptions granted under current § 1.47 will be able to continue to rely on such exemptions for existing positions under reproposed § 150.3(f). Between the December 2013 proposal and now, the Commission has determined to expand the relief in reproposed § 150.3(f). As more fully discussed above, the Commission amended the regulatory text so that previously-granted exemptions may apply to pre-existing financial instruments, rather than only to pre-existing swaps, and to exchange-granted, non-enumerated exemptions in non-legacy commodity derivatives outside of the spot month, with other conditions. The Commission believes that there will be recordkeeping costs but there also will be cost-savings in the form of market stability because market participants will not be required to liquidate positions prematurely, and the relief covers financial instruments not just swaps.

vii. Section 150.3(g) and (h)—Recordkeeping and Special Calls

Under reproposed § 150.3(g) and (h), the costs related to maintaining and producing records will be minimal because, under most circumstances, market participants already maintain books and records in compliance with Commission regulations and as part of prudent accounting and risk management policies and procedures. The Commission has estimated the costs entities might incur and discussed those costs in the PRA section of this release.

6. Section 150.5—Exemptions From Exchange-Set Position Limits

The Dodd-Frank Act scaled back the discretion afforded DCMs for establishing position limits under the earlier CFMA amendments. Specifically, among other things, the Dodd-Frank Act: (1) Amended DCM core principle 5 to require that, with respect to contracts subject to a position limit set by the Commission under CEA section 4a, a DCM must set limits no higher than those prescribed by the Commission;[1348] and (2) added parallel core principle obligations on newly-authorized SEFs, including SEF core principle 6 regarding the establishment of position limits.[1349]

a. Rule Summary

In light of these Dodd-Frank Act statutory amendments, the Commission has adopted § 150.5 to specify certain requirements and guidance for DCMs and SEFs establishing exchange-set limits.

Specifically, § 150.5(a)(1) requires that DCMs and SEFs set position limits for commodity derivative contracts, subject to federal position limits, at a level not higher than the Commission's levels specified in § 150.2. In addition, exchanges with cash-settled contracts price-linked to contracts subject to federal limits must also adopt limit levels not higher than federal position limits.

Further, § 150.5(a)(5) requires for all contracts subject to federal speculative limits, and §§ 150.5(b)(8) and 150.5(c)(8) suggest for other contracts not subject to federal speculative limits, that designated contract markets and swap execution facilities adopt aggregation rules that conform to § 150.4. Regulation § 150.5(a)(2)(i) requires for all contracts subject to federal speculative limits, and

[1346] CL–ICE–59962 at 6–7 (commenter argued that the conditional limit for natural gas "has had no adverse consequences with supply constraints and underlying physical delivery contracts.")

[1347] CL–ICE–59966 at 4–5, CL–ICE–59962 at 5, and CL–IECAssn–59679 at 30.

[1348] Dodd-Frank Act section 735(b). CEA section 4a(e), effective prior to, and not amended by, the Dodd-Frank Act, likewise provides that position limits fixed by a board of trade not exceed federal limits. 7 U.S.C. 6a(e).

[1349] Dodd-Frank Act section 733 (adding CEA section 5h; 7 U.S.C. 7b–3).

regulations §§ 150.5(b)(5)(i)(A) and (c)(5)(1) suggest for other contracts not subject to federal speculative limits, that exchanges conform their bona fide hedging exemption rules to the § 150.1 definition of bona fide hedging position.

Regulation § 150.5(a)(2)(ii) requires, and §§ 150.5(b)(5)(iii) and (c)(5)(iii) suggest that exchanges condition any exemptive relief from federal or exchange-set position limits on an application from the trader. And, if granted an exemption, such trader must reapply for such exemption at least on an annual basis. As noted *supra,* the Commission understands that requiring traders to apply for exemptive relief comports with existing DCM practice; thus, the Commission anticipates that the codification of this requirement will have the practical effect of incrementally increasing, rather than creating, the burden of applying for such exemptive relief.

Finally, under § 150.5(b) and § 150.5(c) for commodity derivative contracts not subject to federal position limits, the Commission provides guidance for exchanges to use their reasonable discretion to set exchange position limits and exempt market participants from exchange-set limits. This includes, under § 150.5(b), commodity derivative contracts in a physical commodity as defined in § 150.1, and, under § 150.5(c), excluded commodity derivative contracts as defined in section 1a(19) of the Act.

b. Baseline

The baseline is the current reasonable discretion afforded to exchanges to exempt market participant from their exchange-set position limits.

c. Benefits and Costs

Functioning as an integrated component within the broader position limits regulatory regime, the Commission expects the proposed changes to § 150.5 will further the four objectives outlined in CEA section 4a(a)(3).[1350] The Commission has endeavored to preserve the status quo baseline within the framework of establishing new federal position limits.

The reproposed regulations require that exchange-set limits employ aggregation policies that conform to the Commission's aggregation policy for contracts that are subject to federal limits under § 150.2, thus harmonizing aggregation rules for all federal and exchange-set speculative position limits. For contracts subject to federal speculative position limits under § 150.2, the Commission anticipates that a harmonized approach to aggregation will prevent confusion that otherwise might result from allowing divergent standards between federal and exchange-set limits on the same contracts. Further, the harmonized approach to aggregation policies for limits on all levels eliminates the potential for exchanges to use permissiveness in aggregation policies as a competitive advantage, which would impair the effectiveness of the Commission's aggregation policy. In addition, DCMs and SEFs are required to set position limits at a level not higher than that set by the Commission. Differing aggregation standards may have the practical effect of increasing a DCM- or SEF-set limit to a level that is higher than that set by the Commission. Accordingly, harmonizing aggregation standards reinforces the efficacy and intended purpose of §§ 150.5(a)(2)(ii), (b)(5)(iii) and (c)(5)(iii) by foreclosing an avenue to circumvent applicable limits. Moreover, by extending this harmonized approach to contracts not included in § 150.2, the Commission encourages a common standard for all federal and exchange-set limits. The adopted rule provides uniformity, consistency, and certainty for traders who are active on multiple trading venues, and thus should reduce the administrative burden on traders as well as the burden on the Commission in monitoring the markets under its jurisdiction.

With respect to exchange-set limits, DCM and SEF core principles already address the costs associated with the requirement that exchanges set position limits no higher than federal limits. Further, for commodity derivatives contracts subject to federal position limits, exchanges are provided the discretion to decide whether or not to set position-limits that are lower than the federal position limit. Finally, when an exchange grants an exemption from a lower exchange-set limit, it is not required to use the Commission's bona fide hedging position definition so long as the exempted position does not exceed the federal position limit.

To the extent that a DCM or SEF grants exemptions, the Commission anticipates that exchanges and market participants will incur minimal costs to administer the application process for exemption relief in accordance with standards set forth in the proposed rule. The Commission understands that requiring traders to apply for exemptive relief comports with existing DCM practice. Accordingly, by incorporating an application requirement that the Commission has reason to understand most if not all active DCMs already follow, the impact of the potential costs has been reduced because the nature of the exemption process is similar to what DCMs already have in place. For SEFs, the rules necessitate a compliant application regime, which will require an initial investment similar to that which DCMs have likely already made and need not duplicate. As noted above, the Commission considers it highly likely that, in accordance with industry best practices, to comply with core principles and due to the utility of application information in demonstrating compliance with core principles, SEFs may incur such costs with or without the adopted rules. Again, due to the new existence of these entities, the Commission is unable to estimate what costs may be associated with the requirement to impose an application regime for exemptive relief on the exchange level.

Also, with respect to phasing, exchanges are not required to use the Commission's definition of bona fide hedging position when setting positon limits on commodity derivative contracts in a physical commodity that are not subject to federal position limits (and when exchanges grant an exemption from exchange-set limits if such exemption does not exceed the federal limit) or excluded commodity derivative contracts. Nevertheless, exchanges are free to use the Commission's bona fide hedging position definition if they so choose.

Relative to the status quo baseline, this rulemaking imposes a ceiling on exchange-set position limits for referenced contracts in 25 commodities. The core principals already require such ceiling, and such costs are addressed in the part 37 and 38 rulemakings. As mandated and necessary, this rule adopts limits for 16 additional commodities. In addition, market participants may be facing hard position limits on some contract that previously only had accountability levels. As such, this rulemaking will confer any benefits that hard position limits have over accountability levels. This may include information gleaned from exemption applications that will better inform the supervisory functions of DCMs or SEFs as well as to protect markets from any adverse effects from market participants that hold positions in excess of an exchange set position limit. In addition, exchanges retain the ability to set accountability levels lower than the levels of the position limits; if an exchanges chooses to adopt such accountability levels, they would

[1350] CEA section 4a(a)(3)(B) applies for purposes of setting federal limit levels. 7 U.S.C. 6a(a)(3)(B). The Commission considers the four factors set out in the section relevant for purposes of considering the benefits and costs of these amendments addressed to exchange-set position limits as well.

provide exchanges with additional information regarding positions of various market participants.

Exchanges and market participants will have to adapt to new federal position limits. Position limits will alter the way that swap and futures trading is conducted. For many contracts that did not have federal limits, participants will be facing new exchange set position limits in the spot, single month, and all months combined. Such limits may impose new compliance costs on exchanges and market participants. These compliance costs may consists of adapting the method of aggregating contracts and filing for exchange exemptions to position limits. The Commission anticipates that these costs will be higher for contracts that have only had accountability levels and not hard exchange-set position limits. Exchange-set position limits may also deter some speculators from fully participating and affecting the price of some futures contracts. The Commission expects that for the most part, exchange-set position limits will not have much effect except for rare circumstances when exemptions to exchange set limits do not apply or other derivative contracts such as swap contracts (below the federal limit), forwards, or trade options are not adequate to meet a market participant's needs.

d. Response to Commenter

A commenter asked whether the Supplemental Proposal's cost-benefit analysis assesses the appropriateness of such requirement on exchange-set speculative position limits or includes the costs of processing non-enumerated bona fide hedging positions and Spread Exemptions for contracts subject only to exchange-set speculative position limits and not federal speculative position limits.[1351]

The Commission notes that if an exchange elects to set a position limit lower than a federal limit, the costs resulting from such choices are not imposed by § 150.5, because the exchange has made the choice not the Commission. The costs on market participants to apply for exchange set limits below the federal level are also discussed in § 150.2. The Commission is unable to forecast these costs, because it does not know when an exchange will set its limits lower than the federal limit; nor does it know how low any such exchange-set position limit level may be.

This rulemaking maintains the status quo for exchange-set speculative limits for contracts not subject to federal limits. Therefore, there are no costs and benefits resulting from this rulemaking on the processing of such exemptions.

7. Section 150.7—Reporting Requirements for Anticipatory Hedging Positions

a. Rule Summary

The revised definition of bona fide hedging position reproposed in § 150.1 of this rule incorporates hedges of five specific types of anticipated transactions: Unfilled anticipated requirements, unsold anticipated production, anticipated royalties, anticipated service contract payments or receipts, and anticipatory cross-hedges.[1352] The Commission is reproposing new requirements in § 150.7 for traders seeking an exemption from position limits for any of these five enumerated anticipated hedging transactions that were designed to build on, and replace, the special reporting requirements for hedging of unsold anticipated production and unfilled anticipated requirements in current § 1.48.[1353]

The Commission proposed to add a new series '04 reporting form, Form 704, to effectuate these additional and updated reporting requirements for anticipatory hedges. Persons wishing to avail themselves of an exemption for any of the anticipatory hedging transactions enumerated in the updated definition of bona fide hedging position in § 150.1 would be required to file an initial statement on Form 704 with the Commission at least ten days in advance of the date that such positions would be in excess of limits established in § 150.2.

Reproposed § 150.7(f) adds a requirement for any person who files an initial statement on Form 704 to provide annual updates that detail the person's actual cash market activities related to the anticipated exemption. Reproposed § 150.7(g) enables the Commission to review and compare the actual cash activities and the remaining unused anticipated hedge transactions by requiring monthly reporting on Form 204.

As is the case under current § 1.48, reproposed § 150.7(h) required that a trader's maximum sales and purchases must not exceed the lesser of the approved exemption amount or the trader's current actual anticipated transaction.

b. Baseline

The baseline is current § 1.48.

c. Benefits and Costs

The Commission remains concerned that distinguishing whether an over-the-limit position is entered into in order to reduce risk arising from anticipatory needs, or whether it is excess speculation, may be exceedingly difficult if anticipatory transactions are not well defined. The Commission is, therefore, reproposing the collection of Form 704 to collect information that is vital in performing this distinction. While there will be costs associated with fulfilling obligations related to anticipatory hedging, the Commission believes that advance notice of a trader's intended maximum position in commodity derivative contracts to offset anticipatory risks would identify—in advance—a position as a bona fide hedging position, avoiding unnecessary contact during the trading day with surveillance staff to verify whether a hedge exemption application is in process, the appropriate level for the exemption and whether the exemption is being used in a manner that is consistent with the requirements. Market participants can anticipate hedging needs well in advance of assuming positions in derivatives markets and in many cases need to supply the same information after the fact; in such cases, providing the information in advance allows the Commission to better direct its efforts towards deterring and detecting manipulation. The annual updates in § 150.7(d) similarly allow the Commission to verify on an ongoing basis that the person's anticipated cash market transactions, estimated in good faith, closely track that person's real cash market activities. Absent monthly filing pursuant to § 150.7(e), the Commission would need to issue a special call to determine why a person's commodity derivative contract position is, for example, larger than the pro rata balance of her annually reported anticipated production. The Commission believes it is reproposing a low cost method of obtaining the necessary information to ensure that anticipatory hedges are valid.[1354]

d. Summary of Comments

One commenter asserted that the reporting requirements for anticipatory hedges of an operational or commercial

[1351] CL–Working Group–60947 at 14.

[1352] *See* paragraphs 3(iii), 4(i), 4(iii), 4(iv) and (5), respectively, of the Commission's definition of bona fide hedging position in § 150.1 as discussed *supra.*

[1353] *See* 17 CFR 1.48. *See also* definition of bona fide hedging transactions in current 17 CFR 1.3(z)(2)(i)(B) and (ii)(C), respectively.

[1354] The Commission understands that there will be costs associated with the filing of Form 704. Costs of filing that form are discussed in the context of the part 19 requirements as well as in the Paperwork Reduction Act section of this release.

risk comprising an initial, supplementary and annual report are unduly burdensome. The commenter recommended that the Commission require either an initial and annual report or an initial and supplementary report.[1355] Another commenter agreed that the proposed requirements to file Forms 204, 704 and/or 604 ''are unduly burdensome and commercially impracticable,'' and stated that the Commission should ''scale back both the frequency and the content of the filings required to maintain bona fide hedge positions.'' [1356]

Another commenter suggested deleting Form 704 because it believes that no matter how extensive the Commission makes reporting requirements, the Commission will still need to request additional information on a case-by-case basis to ensure hedge transactions are legitimate.[1357] The commenter suggested that the Commission should be able to achieve its goal of obtaining enough information to determine whether to request additional information using Form 204 along with currently collected data sources and so the additional burden of the new series '04 reports outweighs the benefit to the Commission.[1358]

Several commenters remarked on the cost associated with Form 704. One commenter stated that the additional reporting requirements, including new Form 704 to replace the reporting requirements under current rule 1.48, and annual and monthly reporting requirements under rules 150.7(f) and 150.7(g) ''will impose significant additional regulatory and compliance burdens on commercials;'' the commenter believes that the Commission should consider alternatives, including targeted special calls when appropriate.[1359] Another commenter stated the reporting requirements for the series 04 forms is overly burdensome and would impose a substantial cost to market participants because while the proposal would require the Commission to respond fairly quickly, it does not provide an indication of whether the Commission will deem the requirement accepted if the Commission does not respond within a stated time frame. The commenter is concerned that a market participant may have to refuse business if it does not receive an approved exemption in advance of a transaction.[1360] A third commenter stated that Form 704 is ''commercially impracticable and unduly burdensome'' because it would require filers to ''analyze each transaction to see if it fits into an enumerated hedge category.'' The commenter is concerned that such ''piecemeal review'' would require a legal memorandum and the development of new software to track positions and, since the Commission proposed that Form 704 to be used in proposed § 150.11, the burden associated with the form has increased.[1361]

Finally, a commenter stated that the Commission significantly underestimated costs associated with reporting, and provided revised estimates of start-up and ongoing compliance costs for filing Form 704.[1362]

As discussed in the December 2013 Position Limits Proposal, the Commission remains concerned about distinguishing between anticipatory reduction of risk and speculation.[1363] Therefore, the Commission is retaining the requirement to file Form 704 for anticipatory hedges. The Commission notes that most of the information required on Form 704 is currently required under § 1.48, and that such information is not found in any other Commission data source, including Form 204.

The Commission is adopting the commenters' suggestions, however, to reduce the frequency of filings by maintaining the requirement for the initial statement and annual update but eliminating the supplemental filing as proposed in § 150.7(e). After considering the commenter's concerns, the Commission believes the monthly reporting on Form 204 and annual updates on Form 704 will provide sufficient updates to the initial statement and is deleting the supplemental filing provision in proposed § 150.7(e) to reduce the burden on filers. The Commission has made several burden-reducing changes to Form 704 and § 150.7(d), including merging the initial statement and annual update sections of Form 704, clarifying and amending the instructions to Form 704, and eliminating redundant information.[1364]

In response to the commenter who suggested the Commission consider targeted special calls and other alternatives to the annual and monthly filings, the Commission believes these filings are critical to the Commission's Surveillance program. Anticipatory hedges, because they are by definition forward-looking, require additional detail regarding the firm's commercial practices in order to ensure that a firm is not using the provisions in proposed § 150.7 to evade position limits. In contrast, special calls are backward-looking and would not provide the Commission's Surveillance program with the information needed to prevent markets from being susceptible to excessive speculation. However, the Commission expects the new filing requirements to be an improvement over current practice under § 1.48 because as facts and circumstances change, the Commission's Surveillance program will have a more timely understanding of the market participant's hedging needs.

The Commission notes in response to the commenter that there is no requirement to analyze individual transactions or submit a memorandum. Finally, while costs of filing Form 704 are discussed below in the context of part 19, the Commission notes that changes made to the frequency of the forms should help alleviate some of the cost burdens associated with filing Form 704.

8. Part 19—Reports

CEA Section 4i authorizes the Commission to require the filing of reports, as described in CEA section 4g, when positions equal or exceed position limits. Current part 19 of the Commission's regulations sets forth these reporting requirements for persons holding or controlling reportable futures and option positions that constitute bona fide hedging positions as defined in § 1.3(z) and in markets with federal speculative position limits—namely those for grains, the soy complex, and cotton. Since having a bona fide hedging position exemption affords a commercial market participant the opportunity to hold positions that exceed a position limit level, it is important for the Commission to be able to verify that, when an exemption is invoked, that it is done so for legitimate purposes. As such, commercial entities that hold positions in excess of those limits must file information on a monthly basis pertaining to owned stocks and purchase and sales commitments for entities that claim a bona fide hedging position exemption.

In order to help ensure that the additional exemptions described in § 150.3 are used in accordance with the requirements of the exemption

[1355] CL–IECAssn–59679 at 11.

[1356] CL–BG Group–59656 at 11.

[1357] CL–NGFA–60941 at 7–8.

[1358] *Id.*

[1359] CL–APGA–59722 at 10.

[1360] CL–EDF–59961 at 6.

[1361] CL–EEI–EPSA–60925 at 9.

[1362] CL–FIA at 35–36.

[1363] *See* December 2013 Position Limits Proposal, 78 FR at 75746.

[1364] *See, supra,* discussion of changes to Form 704 and § 150.7.

employed, as well as obtain information necessary to verify that any futures, options and swaps positions established in referenced contracts are justified, the Commission is making conforming and substantive amendments to part 19. First, the Commission is amending part 19 by adding new and modified cross-references to proposed part 150, including the new definition of bona fide hedging position in reproposed § 150.1.[1365] Second, the Commission is amending § 19.00(a) by extending reporting requirements to any person claiming any exemption from federal position limits pursuant to reproposed § 150.3. The Commission is adding three new series '04 reporting forms to effectuate these additional reporting requirements. Third, the Commission is updating the manner of part 19 reporting. Lastly, the Commission is updating both the type of data that would be required in series '04 reports, as well as the time allotted for filing such reports.

Below, the Commission describes each of the proposed changes; responds to commenters; and considers the costs and benefits of such changes.[1366]

a. Amendments to Part 19

In the December 2013 Position Limits Proposal, the Commission proposed to amend part 19 so that it would conform to the Commission's proposed changes to part 150.[1367] The proposed conforming amendments included: Amending part 19 by adding new and modified cross-references to proposed part 150, including the new definition of bona fide hedging position in proposed § 150.1; updating § 19.00(a) by extending reporting requirements to any person claiming any exemption from federal position limits pursuant to proposed § 150.3; adding new series '04 reporting forms to effectuate these additional reporting requirements; updating the manner of part 19 reporting; and updating both the type of data that would be required in series '04 reports as well as the timeframe for filing such reports.

b. Baseline

The baseline is current part 19.

c. Summary of Comments

The Commission received several comments regarding the general nature of series '04 reports and/or the manner in which such reports are required to be filed. One commenter stated that the various forms required by the regime, while not lengthy, represent significant data collection and categorization that will require a non-trivial amount of work to accurately prepare and file. The commenter claimed that a comprehensive position limits regime could be implemented with a ''far less burdensome'' set of filings and requested that the Commission review the proposed forms and ensure they are ''as clear, limited, and workable'' as possible to reduce burden. The commenter stated that it is not aware of any software vendors that currently provide solutions that can support a commercial firm's ability to file the proposed forms.[1368] Another commenter supports the Commission's decision to require applications for risk management exemptions but requests the Commission to reevaluate the cost the forms will impose such as new compliance programs, training of staff, and purchasing or modifying data management systems in order to meet and maintain the compliance requirements.[1369]

Several commenters requested that the Commission create user-friendly guidebooks for the forms so that all entities can clearly understand any required forms and build the appropriate systems to file such forms, including providing workshops and/or hot lines to improve the forms.[1370]

Finally, two commenters recommended modifying or removing the requirement to certify series '04 reports as ''true and correct.'' One commenter suggested that the requirement be removed due to the difficulty of making such a certification and the fact that CEA section 6(c)(2) already prohibits the submission of false or misleading information.[1371] Another noted that the requirement to report very specific information relating to hedges and cash market activity involves data that may change over time. The commenter suggested the Commission adopt a good-faith standard regarding ''best effort'' estimates of the data when verifying the accuracy of Form 204 submissions.[1372]

The Commission is reproposing the amendments to part 19. The Commission agrees with the commenters that the forms should be clear and workable, and offers several clarifications and amendments in other sections of this release in response to comments about particular aspects of the series '04 reports.[1373]

The Commission notes that the information required on the series '04 reports represents a trader's most basic position data, including the number of units of the cash commodity that the firm has purchased or sold, or the size of a swap position that is being offset in the futures market. The Commission believes this information is readily available to traders, who routinely make trading decisions based on the same data that is required on the series '04 reports. The Commission is moving to an entirely electronic filing system, allowing for efficiencies in populating and submitting forms that require the same information every month. Most traders who are required to file the series '04 reports must do so for only one day out of the month, further lowering the burden for filers. In short, the Commission believes potential burdens have been reduced while still providing adequate information for the Commission's Surveillance program. For market participants who may require assistance in monitoring for speculative position limits and gathering the information required for the series '04 reports, the Commission is aware of several software companies who, prior to the vacation of the Part 151 Rulemaking, produced tools that could be useful to market participants in fulfilling their compliance obligations under the new position limits regime.

In response to the commenters that requested guidebooks for the series '04 reporting forms, the Commission has revised the series '04 forms and the instructions to such forms as discussed *supra* in this release. The Commission believes that it is less confusing to ensure that form instructions are clear and detailed than it is to provide generalized guidebooks that may not respond to specific issues. The Commission's longstanding experience with collecting and reviewing Form 204 and Form 304 has shown that many questions about the series '04 reports are specific to the circumstances and trading strategies of an individual

[1365] These amendments are non-substantive conforming amendments and do not have implications for the Commission's consideration of costs and benefits.

[1366] The Commission notes that comments related to costs and benefits are described in this section, and other comments regarding these provisions are discussed in the section *supra* that describes the reproposed rules for part 19. For a complete picture of the comments received, the Commission's response to comments, and the reproposed rules, all sections of this preamble should be read together.

[1367] *See* December 2013 Position Limits Proposal, 78 FR at 75741–46.

[1368] CL–COPE–59662 at 24, CL–COPE–60932 at 10. *See also* CL–EEI–EPSA–60925 at 9.

[1369] CL–EDF–59961 at 6–7.

[1370] *See* CL–COPE–59662 at 24, CL–COPE–60932 at 10; CL–ASR–60933 at 4; CL–Working Group–60947 at 17–18; CL–EEI–EPSA–60925 at 3.

[1371] *See*, CL–CMC–59634 at 17.

[1372] CL–Working Group–59693 at 65.

[1373] *See, supra,* discussion of reproposed rules regarding series '04 reports and part 19.

market participant, and do not lend themselves to generalization that would be helpful to many market participants. The Commission notes that, should a market participant have questions regarding how to file a particular form, they are encouraged to contact Commission staff directly to get answers tailored to their particular circumstances.

Finally, the Commission is amending the certification language found at the end of each form to clarify that the certification requires nothing more than is already required of market participants in CEA section 6(c)(2). The Commission believes the certification language is an important reminder to reporting traders of their responsibilities to file accurate information under several sections of the Act, including but not limited to CEA section 6(c)(2).

d. Information Required on Series '04 Reports

i. Bona Fide Hedgers Reporting on Form 204—§ 19.01(a)(3)

Current § 19.01(a) sets forth the data that must be provided by bona fide hedgers (on Form 204) and by merchants and dealers in cotton (on Form 304). The Commission proposed to continue using Forms 204 and 304, which will feature only minor changes to the types of data to be reported under § 19.01(a)(3).[1374] These changes include removing the modifier ''fixed price'' from ''fixed price cash position;'' requiring cash market position information to be submitted in both the cash market unit of measurement (*e.g.,* barrels or bushels) and futures equivalents; and adding a specific request for data concerning open price contracts to accommodate open price pairs. In addition, the monthly reporting requirements for cotton, including the granularity of equity, certificated and non-certificated cotton stocks, would be moved to Form 204, while weekly reporting for cotton would be retained as a separate report made on Form 304 in order to maintain the collection of data required by the Commission to publish its weekly public cotton ''on call'' report.

One commenter suggested that the costs to industry participants in collecting and submitting Form 204 data and to the Commission in reviewing it ''greatly outweigh'' the regulatory benefit. The commenter recommended that the Commission undertake a cost-benefit analysis to reconsider what information is required to be provided under part 19 and on Form 204 and limit that information only to what will assist Commission staff in assessing the validity of claimed hedge exemptions.[1375]

One commenter stated that CFTC should reduce the complexity and compliance burden of bona fide hedging record keeping and reporting by using a model similar to the current exchange-based exemption process.[1376] The commenter also stated that the requirement to keep records and file reports, in futures equivalents, regarding the commercial entity's cash market contracts and derivative market positions on a real-time basis globally, will be complex and impose a significant compliance burden. The commenter noted such records are not needed for commercial purposes.[1377]

Another commenter recommended that the Commission should require a market participant with a position in excess of a spot-month position limit to report on Form 204 only the cash-market activity related to that particular spot-month derivative position, and not to require it to report cash-market activity related to non-spot-month positions where it did not exceed a non-spot-month position limit; the commenter stated that the burden associated with such a reporting obligation would increase significantly.[1378]

One commenter recommended that reporting rules require traders to identify the specific risk being hedged at the time a trade is initiated, to maintain records of termination or unwinding of a hedge when the underlying risk has been sold or otherwise resolved, and to create a practical audit trail for individual trades, to discourage traders from attempting to mask speculative trades under the guise of hedges.[1379]

The Commission recognizes that market participants will incur costs to file Form 204; these costs are described in detail below. However, the Commission believes that the costs of filing Form 204 are not overly burdensome for market participants, most of whom currently file similar information with either the Commission or the exchanges in order to obtain and maintain exemptions from speculative position limits. The Commission believes it is reproposing requirements for Form 204 that provide the Commission with the most basic information possible to ascertain the veracity of claimed bona fide hedging positions. The Commission has in some cases accepted commenter suggestions to reduce or amend the information required in order to reduce confusion and alleviate burden on filers.[1380] Where the Commission has retained required information fields, the Commission believes, based on its longstanding experience conducting surveillance in the markets it oversees, that such fields are necessary to determine the legitimacy of claimed bona fide hedging position exemptions.

The Commission notes that, while the exchange referred to by the commenter does not have a reporting process analogous to Form 204, it does require an application prior to the establishment of a position that exceeds a position limit. In contrast, advance notice is not required for most federal enumerated bona fide hedging positions.[1381] In the Commission's experience, the series '04 reports have been useful and beneficial to the Commission's Surveillance program and the Commission finds no compelling reason to change the forms to conform to the exchange's process. Further, the Commission notes that Form 204 is filed once a month as of the close of business of the last Friday of the month; it is not and has never been required to be filed on a real-time basis globally. A market participant only has to file Form 204 if it is over the limit at any point during the month, and the form requires only cash market activity (not derivatives market positions).

The Commission has never distinguished between spot-month limits and non-spot-month limits with respect to the filing of Form 204. The Commission notes that, as discussed in the December 2013 Position Limits Proposal, Form 204 is used to review positions that exceed speculative limits in general, not just in the spot-month.[1382] Because of this, the Commission is proposing not to adopt the commenter's recommendation to

[1374] The list of data required for persons filing on Forms 204 and 304 has been relocated from current § 19.01(a) to reproposed § 19.01(a)(3).

[1375] CL–Working Group–60396 at 17–18.

[1376] CL–ASR–59668 at 3.

[1377] *Id.* at 7. *See also* CL–ASR–60933 at 5.

[1378] CL–FIA–59595 at 38.

[1379] CL–Sen. Levin–59637 at 8.

[1380] *See supra* the Commission's determinations regarding part 19

[1381] The Commission notes that advance notice is required for recognition of anticipatory hedging positions by the Commission. *See supra* for more discussion of anticipatory hedging reporting requirements.

[1382] The Commission stated that the Form 204 ''must show the trader's positions in the cash market and are used by the Commission to determine whether a trader has sufficient cash positions that justify futures and option positions above the speculative limits'' because the Commission is seeking to ''ensure that any person who claims any exemption from federal speculative position limits can demonstrate a legitimate purpose for doing so.'' *See* December 2013 Position Limits Proposal, 78 FR at 75741–42.

only require Form 204 when a market participant exceeds a spot-month limit.

In response to the commenter who suggested the Commission require a ''practical audit trail'' for bona fide hedgers, the Commission notes that other sections of the Commission's regulations provide rules regarding detailed individual transaction recordkeeping as suggested by the commenter.

ii. Conditional Spot-Month Limit Exemption Reporting on Form 504—§ 19.01(a)(1)

As proposed, § 19.01(a)(1) would require persons availing themselves of the conditional spot-month limit exemption (pursuant to proposed § 150.3(c)) to report certain detailed information concerning their cash market activities for any commodity specially designated by the Commission for reporting under § 19.03 of this part. In the December 2013 Position Limits Proposal, the Commission noted its concern about the cash market trading of those availing themselves of the conditional spot-month limit exemption and so proposed to require that persons claiming a conditional spot-month limit exemption must report on new Form 504 daily, by 9 a.m. Eastern Time on the next business day, for each day that a person is over the spot-month limit in certain special commodity contracts specified by the Commission.

The Commission proposed to require reporting on new Form 504 for conditional spot-month limit exemptions in the natural gas commodity derivative contracts only, until the Commission gains additional experience with the limits in proposed § 150.2 in other commodities as well.

Benefits and Costs

The reporting requirements allow the Commission to obtain the information necessary to verify whether the relevant exemption requirements are fulfilled in a timely manner. This is needed for the Commission to help ensure that any person who claims any exemption from federal speculative position limits can demonstrate a legitimate purpose for doing so. In the absence of the reporting requirements detailed in part 19, the Commission would lack critical tools to identify abuses related to the exemptions afforded in § 150.3 in a timely manner. As such, the reporting requirements are necessary for the Commission to be able to perform its essential surveillance functions. These reporting requirements therefore promote the Commission's ability to achieve, to the maximum extent practicable, the statutory factors outlined by Congress in CEA section 4a(a)(3).

The Commission recognizes there will be costs associated with the changes and additions to the report filing requirements under part 19. Though the Commission anticipates that market participants should have ready access to much of the required information, the Commission expects that, at least initially, market participants will require additional time and effort to become familiar with new and amended series '04 forms, to gather the necessary information in the required format, and to file reports in the proposed timeframes. As described above, the Commission has attempted to mitigate the cost impacts of these reports.

Actual costs incurred by market participants will vary depending on the diversity of their cash market positions and the experience that the participants currently have regarding filing Form 204 and Form 304 as well as a variety of other organizational factors. However, the Commission has estimated average incremental burdens associated with the proposed rules in order to fulfill its obligations under the Paperwork Reduction Act (''PRA'').[1383]

For Form 204, the Commission estimates that approximately 425 market participants will file an average of 12 reports annually at an estimated labor burden of 3 hours per response for a total per-entity hour burden of approximately 36 hours, which computes to a total annual burden of 15,300 hours for all affected entities. Using an estimated hourly wage of $122 per hour,[1384] the Commission estimates an annual per-entity cost of approximately $4,392 and a total annual cost of $1,866,600 for all affected entities. These estimates are summarized below in Table IV–A–1.

TABLE IV–A–1—BURDEN ESTIMATES FOR FORM 204

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Form 204 | 425 | 3 | 12 | $122.00 | $4,392 |

For Form 304, the Commission estimates that approximately 200 market participants will file an average of 52 reports annually at an estimated labor burden of 1 hour per response for a total per-entity hour burden of approximately 52hours, which computes to a total annual burden of 10,400 hours for all affected entities. Using an estimated hourly wage of $122 per hour, the Commission estimates an annual per-entity cost of approximately $6,344 and a total annual cost of $1,268,800 for all affected entities. These estimates are summarized below in Table IV–A–2.

[1383] *See supra* for discussion of the Commission's Paperwork Reduction Act estimates and explanation.

[1384] The Commission's estimates concerning the wage rates are based on 2011 salary information for the securities industry compiled by the Securities Industry and Financial Markets Association (''SIFMA''). The Commission is using $122 per hour, which is derived from a weighted average of salaries across different professions from the SIFMA Report on Management & Professional Earnings in the Securities Industry 2013, modified to account for an 1800-hour work-year, adjusted to account for the average rate of inflation since 2013, and multiplied by 1.33 to account for benefits and 1.5 to account for overhead and administrative expenses. The Commission anticipates that compliance with the provisions would require the work of an information technology professional; a compliance manager; an accounting professional; and an associate general counsel. Thus, the wage rate is a weighted national average of salary for professionals with the following titles (and their relative weight); ''programmer (senior)'' and ''programmer (non-senior)'' (15% weight), ''senior accountant'' (15%) ''compliance manager'' (30%), and ''assistant/associate general counsel'' (40%). All monetary estimates have been rounded to the nearest hundred dollars.

TABLE IV–A–2—BURDEN ESTIMATES FOR FORM 304

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Form 304 | 200 | 1 | 52 | $122.00 | $6,344 |

For Form 504, the Commission estimates that approximately 40 market participants will file an average of 12 reports annually at an estimated labor burden of 15 hours per response for a total per-entity hour burden of approximately 180 hours, which computes to a total annual burden of 7,200 hours for all affected entities. Using an estimated hourly wage of $122 per hour, the Commission estimates an annual per-entity cost of approximately $21,960 and a total annual cost of $878,400 for all affected entities. These estimates are summarized below in Table IV–A–3.

TABLE IV–A–3—BURDEN ESTIMATES FOR FORM 504

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Form 504 | 40 | 15 | 12 | $122.00 | $21,960 |

For Form 604 filed outside of the spot month, the Commission estimates that approximately 250 market participants will file an average of 10 reports annually at an estimated labor burden of 30 hours per response for a total per-entity hour burden of approximately 300 hours, which computes to a total annual burden of 75,000 hours for all affected entities. Using an estimated hourly wage of $122 per hour, the Commission estimates an annual per-entity cost of approximately $36,600 and a total annual cost of $9,150,000 for all affected entities. For Form 604 filed during of the spot month, the Commission estimates that approximately 100 market participants will file an average of 10 reports annually at an estimated labor burden of 20 hours per response for a total per-entity hour burden of approximately 200 hours, which computes to a total annual burden of 20,000 hours for all affected entities. Using an estimated hourly wage of $122 per hour, the Commission estimates an annual per-entity cost of approximately $24,400 and a total annual cost of $2,440,000 for all affected entities. These estimates are summarized below in Table IV–A–4.

TABLE IV–A–4—BURDEN ESTIMATES FOR FORM 604

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Form 604, Non-Spot-Month | 250 | 30 | 10 | $122.00 | $36,600 |
| Form 604, Spot-Month | 100 | 20 | 10 | 122.00 | 24,400 |

For initial statements filed on Form 704, the Commission estimates that approximately 250 market participants will file an average of 1 report annually at an estimated labor burden of 15 hours per response for a total per-entity hour burden of approximately 15 hours, which computes to a total annual burden of 3,750 hours for all affected entities. Using an estimated hourly wage of $122 per hour, the Commission estimates an annual per-entity cost of approximately $1,830 and a total annual cost of $457,500 for all affected entities. For annual updates filed on Form 704, the Commission estimates that approximately 250 market participants will file an average of 1 report annually at an estimated labor burden of 8 hours per response for a total per-entity hour burden of approximately 8 hours, which computes to a total annual burden of 2,000 hours for all affected entities. Using an estimated hourly wage of $122 per hour, the Commission estimates an annual per-entity cost of approximately $976 and a total annual cost of $244,000 for all affected entities. These estimates are summarized below in Table IV–A–5.

TABLE IV–A–5—BURDEN ESTIMATES FOR FORM 704

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Form 704, Initial Statement | 250 | 15 | 1 | $122 | $1,830 |
| Form 704, Annual Update | 250 | 8 | 1 | 122 | 976 |

(2) Summary of Comments

Several commenters seemed not to understand which market participants will be required to file Form 504, as many made comments regarding the burden on bona fide hedgers (who are not required to file Form 504). One commenter stated its belief that the information required on Form 504 is redundant of information required on Form 204 and would overly burden hedgers.[1385] Another commenter stated that Form 504 creates a burden for hedgers to track their cash business and affected contracts and to create systems to file multiple forms. The commenter noted its belief that end-users/hedgers should never be subjected to the daily filing of reports.[1386] Another commenter requested that the Commission change the Proposed Rule to permit market participants that rely on the conditional limit to file monthly bona fide hedging reports rather than a daily filing of all cash market positions because Form 504 would impose significant burdens on commercial market participants with cash market positions, particularly when compared to purely speculative traders who do not hold cash market positions.[1387]

A commenter suggested that the Commission should modify the data requirements for Form 504 in a manner similar to the approach used by ICE Futures U.S. for natural gas contracts, that is, requiring a description of a market participant's cash-market positions as of a specified date filed in advance of the spot-month.[1388]

The Commission notes that there is a key distinction between Form 504 and Form 204. Form 504 is required of speculators that are relying upon the conditional spot-month limit exemption. Form 204 is required for hedgers that exceed position limits. To the extent a firm is hedging, there is no requirement to file Form 504.

In the unlikely event that a firm is both hedging and relying upon the conditional spot-month limit exemption, the firm would be required to file both forms at most one day a month, given the timing of the spot-month in natural gas markets (the only market for which Form 504 will be required). In that event, however, the Commission believes that requiring similar information on both forms should encourage filing efficiencies rather than duplicating the burden. For example, both forms require the filer to identify fixed price purchase commitments; the Commission believes it is not overly burdensome for the same firm to report such similar information on Form 204 and Form 504, should a market participant ever be required to file both forms.

The Commission does not believe that a description of a cash market position is sufficient to allow Commission staff to administer its Surveillance program. Descriptions are not as exact as reported information, and the Commission believes the information gathered in daily Form 504 reports would be more complete—and thus more beneficial—in determining compliance and detecting and deterring manipulation. The Commission reiterates that Form 504 will only be required from participants in natural gas markets who seek to avail themselves of the conditional spot-month limit exemption, limiting the burden to only those participants.[1389]

iii. Time and Place of Filing Reports—§ 19.01(b)

As proposed, § 19.01(b)(1) would require all reports, except those submitted in response to special calls or on Form 504, Form 604 during the spot-month, or Form 704, to be filed monthly as of the close of business on the last Friday of the month and not later than 9 a.m. Eastern Time on the third business day following the last Friday of the month.[1390] For reports submitted on Form 504 and Form 604 during the spot-month, proposed § 19.01(b)(2) would require filings to be submitted as of the close of business for each day the person exceeds the limit during the spot period and not later than 9 a.m. Eastern Time on the next business day following the date of the report.[1391] Finally, proposed § 19.01(b)(3) would require series '04 reports to be transmitted using the format, coding structure, and electronic data transmission procedures approved in writing by the Commission or its designee.

One commenter recommended an annual Form 204 filing requirement, rather than a monthly filing requirement. The commenter noted that because the general size and nature of its business is relatively constant, the differences between each monthly report would be insignificant. The commenter recommended the CFTC ''not impose additional costs of monthly reporting without a demonstration of significant additional regulatory benefits.'' The commenter noted its futures position typically exceeds the proposed position limits, but such positions are bona fide hedging positions.[1392] Similarly, another commenter suggested that if the Commission does not eliminate the forms in favor of the requirements in the 2016 Supplemental Position Limits Proposal the Commission should require only an annual notice that details its maximum cash market exposure that justifies an exemption, to be filed with the exchange.[1393]

One commenter suggested that the reporting date for Form 204 should be the close of business on the day prior to the beginning of the spot period and that it should be required to filed no later than the 15th day of the month following a month in which a filer exceeded a federal limit to allow the market participant sufficient time to collect and report its information.[1394]

With regards to proposed § 19.01(b)(2), one commenter recommended that the Commission change the proposed next-day reporting of Form 504 for the conditional spot-month limit exemption and Form 604 for the pass-through swap offsets during the spot-month, to a monthly basis, noting market participants need time to generate and collect data and verify the accuracy of the reported data. The commenter further stated that the Commission did not explain why it needs the data on Form 504 or Form 604 on a next-day basis.[1395]

Another asserted that the daily filing requirement of Form 504 for participants who rely on the conditional spot-month limit exemption ''imposes significant burdens and substantial costs on market participants.'' The commenter urged a monthly rather than a daily filing of all cash market positions, which the commenter claimed is consistent with current

[1385] CL–Working Group–59693 at 65–66

[1386] CL–COPE–59662 at 24

[1387] *See,* CL–EEI–EPSA–59602 at 10.

[1388] CL–FIA–59595 at 37

[1389] As stated in the December 2013 Position Limits Proposal, the Commission will closely monitor the reporting requirements associated with conditional spot-month limit exemptions in natural gas to determine whether reporting on Form 504 would be appropriate in the future for other commodity derivative contracts in response to market developments or in order to facilitate surveillance efforts. *See* December 2013 Position Limits Proposal, 78 FR at 75744. However, the Commission is not proposing a conditional spot-month limit exemption in any other commodity at this time.

[1390] The timeframe for filing Form 704 is included as part of proposed § 150.7. *See supra* for discussion regarding the filing of Form 704.

[1391] In proposed § 19.01(b)(2), the Commission inadvertently failed to include reports filed under § 19.00(a)(1)(ii)(B) (*i.e.* Form 604 during the spot month) in the same filing timeframe as reports filed under § 19.00(a)(1)(i) (*i.e.* Form 504). The correct filing timeframe was described in multiple places on the forms published in the **Federal Register** as part of the December 2013 Position Limits Proposal.

[1392] CL–DFA–59621 at 2.

[1393] CL–FIA–60937 at 17.

[1394] CL–Working Group–60947 at 17–18

[1395] CL–FIA–59595 at 35.

exchange practices.[1396] Another commenter agreed, claiming that by making the reporting requirement monthly rather than daily, the Commission would balance the costs and benefits associated with Form 504 requirements on market participants relying on the conditional spot month limit.[1397]

In response to the commenters' suggestions that Form 204 be filed annually, the Commission notes that throughout the course of a year, most commodities subject to federal position limits under proposed § 150.2 are subject to seasonality of prices as well as less predictable imbalances in supply and demand such that an annual filing would not provide the Commission's Surveillance program insight into cash market trends underlying changes in the derivative markets. This insight is necessary for the Surveillance program to determine whether price changes in derivative markets are caused by fundamental factors or manipulative behavior. Further, the Commission believes that an annual filing could actually be more burdensome for firms, as an annual filing could lead to special calls or requests between filings for additional information in order for the Commission's Surveillance program to fulfill its responsibility to detect and deter market manipulation. In addition, the Commission notes that while one participant's positions may remain constant throughout a year, the same is not true for many other market participants. The Commission believes that varying the filing arrangement depending on a particular market or market participant is impractical and would lead to increased burdens for market participants due to uncertainty regarding when each firm with a position in a particular commodity derivative would be required to file.

The Commission is retaining the last Friday of the month as the required reporting date in order to avoid confusion and uncertainty, particularly for those participants who already file Form 204 and thus are accustomed to that reporting date.

The Commission is reproposing § 19.01(b)(2) to require next-day, daily filing of Forms 504 and 604 in the spot-month. In response to the commenter, the Commission notes that it described its rationale for requiring Forms 504 and 604 daily during the spot-month in the December 2013 Position Limits Proposal.[1398] In order to detect and deter manipulation during the spot-month, concurrent information regarding the cash positions of a speculator holding a conditional spot-month limit exemption (Form 504) or the swap contract underlying a large offsetting position in the physical-delivery contract (Form 604) is necessary during the spot-month. Receiving Forms 504 or 604 before or after the spot-month period would not help the Surveillance program to protect the price discovery process of physical-delivery contracts and to ensure that market participants have a qualifying pass-through swap contract position underlying offsetting futures positions held during the spot-month.

The Commission notes that Form 504 is required only for the Natural Gas commodity, which has a 3-day spot period. Daily reporting on Form 504 during the spot-month allows the Surveillance program to monitor a market participant's cash market activity that could impact or benefit their derivatives position. Given the short filing period for natural gas and the importance of accurate information during the spot-month, the Commission believes that requiring Form 504 to be filed daily provides an important benefit that outweighs the potential burdens for filers.[1399]

As a practical matter, the Commission notes that Form 604 is collected during the spot-month only under particular circumstances, *i.e.,* for an offset of a cash-settled swap position with a physical-delivery referenced contract during the spot-month. Because the ''five-day rule'' applies to such positions, the spot-month filing of Form 604 would only occur in contracts whose spot-month period is longer than 5 days (excluding, for example, energy contracts, but including many agricultural commodities).

9. Sections 150.9, 150.10, and 150.11—Processes for Recognizing Positions Exempt From Position Limits

The Commission is reproposing the process for recognizing certain market-participant positions as bona fide hedges (§ 150.9), spreads (§ 150.10), and anticipatory bona fide hedges (§ 150.11), so that the positions may be deemed exempt from federal and exchange-set position limits. The Commission invited the public to comment on the Commission's consideration of the costs and benefits of the processes in the 2016 Supplemental Position Limits Proposal, identify and assess any costs and benefits not discussed therein, and provide possible alternative proposals. The Commission received comment letters in 2013 that helped the Commission re-design the exemption-recognition processes and then reproposrepropose them in the 2016 Supplemental Position Limits Proposal. The Commission received more comment letters on the June 2016 proposed exemption-recognition processes and a number of commenters remarked on the costs and benefits.

The general theme of the costs-related comments is that the three, exemption-recognition processes have overly burdensome reporting requirements. And the majority of benefits-related comments expressed that the exchanges are the best positioned entities to assess whether market positions fall within one of the categories of positions exempt from position limits. There also were a few comments asserting that the Commission underestimated the quantified costs, such as staff hours needed to review exemption applications. The Commission is addressing the qualitative and quantitative comments in the discussion that follows. Furthermore, the Commission will explain why it believes, after careful consideration of the comments, that the reproposed exemption-recognition processes will, among other things, improve transparency via exchange- and Commission-reporting, and improve regulatory certainty by having applicants submit materials for review to exchanges, and by having exchanges assess whether positions should be deemed exempt from position limits.

The baseline against which the Commission considers the benefits and costs of the exemption-recognition rules is a combination of CEA requirements and Commission regulations that are now in effect. That is, the general baseline is the Commission's part 150 regulations and current §§ 1.47 and

[1396] CL–ICE–59669 at 7.

[1397] *See* CL–EEI–EPSA–59602 at 10.

[1398] December 2013 Position Limits Proposal, 78 FR at 75744–45. The Commission noted that its experience overseeing the ''dramatic instances of disruptive trading practices in the natural gas markets'' warranted enhanced reporting for that commodity during the spot month on Form 504. The Commission noted its intent to wait until it gained additional experience with limits in other commodities before imposing enhanced reporting requirements for those commodities. The Commission further noted that it was concerned that a trader could hold an extraordinarily large position early in the spot month in the physical-delivery contract along with an offsetting short position in a cash-settled contract (such as a swap), and that such a large position could disrupt the price discovery function of the core referenced futures contract.

[1399] Should the Commission determine in the future to require Form 504 for other commodities, particularly those with longer spot month periods, the Commission will evaluate the daily filing requirement as it applies to such other commodities.

1.48.[1400] For greater specificity, the Commission has identified the specific, associated baseline from which costs and benefits are determined under each discussion of the reproposed exemption rules below.

a. Section 150.9—Exchange Recognition of Non-Enumerated Bona Fide Hedging Positions

Under Section III.G., above, the Commission summarizes the changes it reproposed in rule § 150.9, which outlines the process that exchanges may employ to recognize certain commodity derivative positions as non-enumerated bona fide hedging positions. The reproposed version of § 150.9 closely follows the regulatory text proposed in the June 2016 Supplemental Proposal. Most of the changes are clarifications. There are, however, substantive changes between the regulatory text proposed in June 2016 and the reproposed regulatory text in this Release; they are to the following subsections:

- The exchange-application requirements under § 150.9(a)(1)(v) and § 150.9(a)(3)(ii), (iii), and (iv);
- the applicant-to-exchange, reporting requirement under § 150.9(a)(6); and
- the exchange-to-Commission, reporting requirement under § 150.9(c)(2).

i. Section 150.9(a)—Exchange-Administered Non-Enumerated Bona Fide Hedging Position Application Process

In paragraph (a) of reproposed § 150.9, the Commission identifies the process and information required for an exchange to assess whether it should grant a market participant's request that its derivative position(s) be recognized as an non-enumerated bona fide hedging position. In the reproposed version of § 150.9(a), the Commission clarified a condition in § 150.9(a)(1)(v).[1401] The clarification is that an exchange offering non-enumerated bona fide hedging position exemptions must have at least one year of experience and expertise to administer position limits for a referenced contract rather than experience and expertise in the derivative contract. In reproposed § 150.9(a)(2), the Commission offers guidelines for exchanges to establish adaptable application processes by permitting different processes for ''novel'' versus ''substantially similar'' applications for non-enumerated bona fide hedging position recognitions. Reproposed § 150.9(a)(3) describes in general terms the type of information that exchanges should collect from applicants. The Commission made a material change in reproposed § 150.9(a)(3)(iv) by reducing the amount of cash-market data an applicant must submit to an exchange from three years to one year.[1402] In addition, 150.9(a)(3)(ii) and (iv) were both changed to provide that the exchange need require the ''information'' rather than ''detailed information.'' Reproposed § 150.9(a)(4) obliges applicants and exchanges to act timely in their submissions and notifications, respectively, and that exchanges retain revocation authority. Reproposed § 150.9(a)(5) provides that the position will be deemed recognized as an non-enumerated bona fide hedging position when an exchange recognizes it. Reproposed § 150.9(a)(6) instructs exchanges to determine whether there should be a reporting requirement for non-enumerated bona fide hedging positions. The Commission changed § 150.9(a)(6) to relieve market participants from an additional filing, and to give exchanges discretion on non-enumerated bona fide hedging position reporting. Reproposed § 150.9(a)(7) requires an exchange to publish on their Web site descriptions of unique types of derivative positions recognized as non-enumerated bona fide hedging positions based on novel facts and circumstances.

ii. Section 150.9(b)—Non-Enumerated Bona Fide Hedging Position Recordkeeping Requirements

The Commission made no changes to the rule text in § 150.9(b) between the 2016 supplemental proposal and this Reproposal. Under reproposed § 150.9(b), exchanges will be required to maintain complete books and records of all activities relating to the processing and disposition of non-enumerated bona fide hedging position applications. As explained in reproposed § 150.9(b)(1) through (b)(2), the Commission instructs exchanges to retain applicant-submission materials, exchange notes, and determination documents. Moreover, consistent with current § 1.31, the Commission expects that these records will be readily accessible until the termination, maturity, or expiration date of the bona fide hedge recognition and during the first two years of the subsequent, five-year retention period.

iii. Section 150.9(c)—Non-Enumerated Bona Fide Hedging Positions Reporting Requirements

The Commission made a change to reporting to the rule text in § 150.9(c) between the 2016 supplemental proposal and this Reproposal. While the Commission is reproposing rules requiring weekly reporting obligations by exchanges for positions recognized as non-enumerated bona fide hedging positions, the Commission changed § 150.9(c)(1)(i) and § 150.9(c)(2) for purposes of clarification. In regards to § 150.9(c)(1)(i), the Commission is clarifying that the reports required under (c)(1)(i) are those for each commodity derivatives position that had been recognized that week and for any revocation or modification of a previously granted recognition. The change to § 150.9(c)(2) explains that exchanges must file monthly Commission reports only if the exchange has determined, in its discretion, that applicants should file exchange reports. The Commission also reproposes § 150.9(c)(1)(ii), which provides that exchanges post non-enumerated bona fide hedging position summaries on their Web sites.

iv. Section 150.9(d) and (e)—Commission Review

The Commission made no changes to the rule text in §§ 150.9 (d) or (e) between the 2016 supplemental proposal and this Reproposal. The Commission reproposes rules that states that market participants and exchanges must respond to Commission requests, as well as liquidated positions within a commercially reasonable amount of time if required under § 150.9(d).

v. Section 150.9(f)—Delegation to Director of the Division of Market Oversight

The Commission made no changes to the rule text in § 150.9(f) between the 2016 supplemental proposal and this Reproposal. In the reproposed version of § 150.9(f), the Commission delegates certain review authority for the non-enumerated bona fide hedging position recognition-process to the Director of the Division of Market Oversight.

vi. Baseline

For the non-enumerated bona fide hedging position process, the baseline for non-enumerated bona fide hedging positions subject to federal position limits is current § 1.47. For non-enumerated bona fide hedging position exemptions to exchange-set position limits, the baseline is the current exchange regulations and practices as well as the Commission's guidance to

[1400] *See* chart listing current regulations, December 2013 Position Limits Proposal, 78 FR 75712, Dec. 12, 2013.

[1401] For a fuller discussion of the change, *see* Section III.G.3.a.(i)–(iii).

[1402] For a fuller discussion of the change, *see* Section III.G.3.b.(iii) exchanges in current § 150.5(d). The current rule provides, generally, that an exchange may recognize bona fide hedging positions in accordance with the general definition of bona fide hedging position in current § 1.3(z)(1).

vii. Benefits and Discussion of Comments

The Commission continues to believe that the non-enumerated bona fide hedging position exemption-recognition process outlined in § 150.9 will produce significant benefits. As explained in the 2016 supplemental proposal, the Commission recognizes that there are positions that reduce price risks incidental to commercial operations. For that reason, among others, such positions that are shown to be bona fide hedging positions under CEA Section 4a(c) are not subject to position limits. And, therefore, it is beneficial for market participants to have several options regarding bona fide hedging positions. With this Reproposal, market participants will have three ways in which they may determine that positions are bona fide hedging positions. First, market participants could conclude that a commodity derivative position comports with the definition of bona fide hedging position under § 150.1. Second, market participants may request a staff interpretive letter under § 140.99 or seek exemptive relief under CEA section 4(a)(7). Third, they may file an application with an exchange for recognition of an non-enumerated bona fide hedging position under reproposed § 150.9.

While all of the aforementioned options are viable, the Commission continues to believe that reproposed § 150.9 outlines a framework similar to existing exchange practices that recognize non-enumerated bona fide hedge exemptions to exchange-set limits. These practices are familiar to many market participants. Moreover, a number of commenters agreed that exchanges should oversee the exemption-recognition process.[1403]

The Commission believes that under reproposed § 150.9, the Commission will be able to leverage exchanges' existing practices and expertise in administering exemptions. Thus, reproposed § 150.9 should reduce the need to invent new procedures to recognize non-enumerated bona fide hedging positions. As explained in the 2016 supplemental proposal, exchanges also may be familiar with the applicant-market participant's needs and practices so there will be an advanced understanding for why certain trading strategies are pursued. The Commission received comments that were consistent with this view.

For example, in response to proposed § 150.9(a)(3)(iv)—the rule requiring applicants to submit detailed information regarding the applicant's activity in the cash market during the past three years—there were a few comments. One commenter noted that exchanges should have the discretion to determine the requisite number of years of data that should be collected.[1404] Another commenter proposed that exchanges have the discretion to collect up to one year of data.[1405] A different commenter remarked that proposed § 150.9(a)(3)(iii) (requiring an applicant to identify ''the maximum size of all gross positions in derivative contracts to be acquired by the applicant during the year after the application is submitted'') is unnecessary and unduly burdensome.'' [1406]

These comments support the Commission's determination to reduce filing burdens. In reproposed § 150.9(a)(3)(ii) and (iv), the Commission changed the requirement that the application process require an applicant submit ''detailed information'' in regards to certain information to ''information.'' The change provides the exchanges with the discretion to determine what level of detail is needed to make their determination. The Commission has also reduced the minimum cash market data requirement to one-year from three-years in proposed § 150.9(a)(3)(iv), which will reduce market participants burden in comparison to the proposed rule.[1407] Furthermore, the Commission continues to believe, even with this change to § 150.9(a)(3)(iv), that given the availability of the exchange's analysis and the Commission's macro-view of the markets, the Commission will be well-informed should it become necessary for the Commission to review a determination under reproposed § 150.9(d), and determine whether a commodity derivative position should be recognized as an non-enumerated bona fide hedging position. The Commission also has clarified in reproposed § 150.9(a)(3)(iii) that the filing must include the maximum size of all gross positions for which the application is submitted, which may be a longer time period than the proposed one-year period. In administering requests for recognition of non-enumerated bona fide hedging position exemptions under § 1.47, the Commission has found a maximum size statement, as required under § 1.47(b)(4), to be useful both at the time of review of the filing (in determining whether the requested maximum size is reasonable in relation to past cash market activity) and at the time of review of a filer's position that exceeds the level of the position limit (reducing the need for special calls to inquire as to the reason a position exceeds a position limit level).

In general, the non-enumerated bona fide hedging position recognition process under reproposed § 150.9 should reduce duplicative efforts because applicants will be saved the expense of applying to both an exchange for relief from exchange-set position limits and to the Commission for relief from federal limits. The Commission also seeks to collect relevant information. Thus, because commenters reasonably complained about the application requirement for three years of cash-market position information, the Commission changed the requirement to one year.[1408] Once commenter stated that the three-year data provided ''little practical benefit'' for assessing whether an non-enumerated bona fide hedging position is appropriate.[1409]

Another section where commenters observed redundancy was in proposed § 150.9(a)(6) regarding requirements for exchanges to require applicants to file reports.[1410] One commenter stated that the proposal to require reports ''is particularly problematic due to its vagueness in terms of the frequency that a cash market report must be provided.'' [1411] Another commenter explained further that proposed § 150.9(a)(6) had no ''incremental market surveillance or other regulatory benefit'' because other rules provide for applicants to reapply for exemptions

[1403] *See, e.g.,* CL–CME–60926; CL–Nodal–60948.

[1404] CL–AGA–60943 at 6.

[1405] CL–NCGA/NGSA–60919 at 10.

[1406] CL–Commercial Energy Working Group–60932 at 10.

[1407] It should be noted that this one-year cash-market history is less than the three-year cash-market history required under reproposed § 150.7(d)(1)(iv) for initial statements regarding enumerated anticipatory bona fide hedging positions.

[1408] For a fuller discussion, *see* Section III.G.1.b. *See also* the following comment letters: CL–AGA–60943 at p. 6 (requirement is vague and restrictive); CL–CCI–60935 at p. 7 (one year of data suggested); CL–EEI–EPSA–60925 at p. 10 (requirement is ''unduly burdensome and unnecessary''); CL–NCGA/NGSA–60919 at p. 10 (same); CL–COPE–60932 at p. 9 (criticized the three-year data requirement); CL–Commercial Energy Working Group–60932 at p. 11 (the requirement is unnecessary).

[1409] CL–Commercial Energy Working Group–60932 at 11.

[1410] *See also* CL–Commercial Energy Working Group–60932 at 12 (the same conclusion applies to proposed 105.10(a)(6), and § 150.11(a)(5)).

[1411] CL–AGA–60943 at 6.

annually, real-time market surveillance, the exchanges' abilities to make one-off requests for information, and the Commission's special call authority.[1412] There also was a commenter who stated that ''neither exchanges nor the Commission are likely to have resources available to meaningfully review such reports'' as those under § 150.9(a)(6), as well as those reports under § 105.10(a)(6).[1413] As explained above, the Commission changed the regulatory text so that exchanges may decide whether non-enumerated bona fide hedging position applicants should provide additional reports to exchanges. As a result of this change, market participants may have less reporting requirements but that assessment will depend on whether the exchanges—based on their experiences and expertise in position limits in general and in non-enumerated bona fide hedging positions specifically—decide to grant a non-enumerated bona fide hedging position exemption without establishing a reporting requirement.

As expressed in the 2016 supplemental proposal, the creation and retention of records under § 150.9 may be used as reference material in the future for similar bona fide hedge recognition requests either by relevant exchanges or the Commission. This will be beneficial because retained records will help the Commission to ensure that an exchange's determinations are internally consistent and consistent with the Act and the Commission's regulations thereunder. There is also the additional benefit that records will be accessible if they are needed for a potential enforcement action.

The Commission continues to believe that the exchange-to-Commission reporting under § 150.9(c) will have surveillance benefits. The reports will provide the Commission with notice that an applicant may take a commodity derivative position that the exchange has recognized as an non-enumerated bona fide hedging position, and also will show the applicant's underlying cash commodity and expected maximum size in the cash markets. Reports will facilitate the tracking of non-enumerated bona fide hedging positions recognized by the exchanges, and will assist the Commission in ensuring that a market participant's activities conform to the exchange's terms of recognition and to the Act. While there are great benefits, in reproposed § 150.9(c)(1)(i) and § 150.9(c)(2), the Commission made clarifications that, as noted above, eased the burden on exchanges and applicants. Asreproposed, § 150.9(c)(1)(i) clarifies that the reports required are only for those for each commodity derivatives position that had been recognized that week and for any revocation or modification of a previously granted recognition. In addition, reproposed § 150.9(c)(2) defers to the exchanges by clarifying that they have the discretion to determine whether a market participant must report under reproposed § 150.9(a)(6); however, if an exchange requires reports of a market participant, that exchange must forward any such report to the Commission under reproposed § 150.9(c)(2). This gives the exchanges flexibility and defers to their expertise. The web-posting of summaries also will benefit market participants in general by providing transparency and open access to the non-enumerated bona fide hedging position recognition process. In addition, reporting and posting gives market participants seeking recognition of a non-enumerated bona fide hedging position an understanding of the types of commodity derivative positions an exchange may recognize as an non-enumerated bona fide hedging position, thereby providing greater administrative and legal certainty.

viii. Costs and Discussion of Comments

In the June 2016 Supplemental Proposal, the Commission explained that to a large extent, exchanges and market participants have incurred already many of the compliance costs associated with the proposed exemptions. The Commission, however, detailed a number of the readily-quantifiable costs for exchanges and market participants associated with processing non-enumerated bona fide hedging position recognitions, as well as spreads and anticipatory bona fide hedges. The Commission invited public comment on the estimated financial numbers, which were detailed in tables. Several commenters remarked on the costs the Commission quantitatively estimated in the June 2016 Supplemental Proposal. One group commenter stated that the Commission underestimated costs to market participants.[1414] The same commenter explained that the Commission failed to ''break out the costs for submitting an initial application and filing subsequent updates every time information in the application changes.''[1415] Another commenter stated that the 2016 Supplemental Proposal has ''highly unrealistic estimates of the time and cost that will be required to implement and maintain compliance programs.''[1416]

One exchange commenter declared that the Commission ''significantly underestimates the number of exemptions that the Exchange will be required to review,'' and offered different numbers.[1417] For example, the exchange commenter stated that it reviewed as many as 500 exemption requests annually as opposed to the 285 exemption requests that the Commission estimated.[1418] In addition, the exchange commenter stated that the Commission underestimated the number of staff-review hours, and that the number should be two additional hours for a total of seven hours per exemption review.[1419] The exchange commenter also provided different hours for different exercises: (a) Seven hours for preparing quarterly Web site postings; (b) six hours for preparation for weekly reports; and (c) six hours for preparing monthly reports.[1420] The exchange commenter also explained that it believed it would need to hire a seasoned, senior level employee to help comply with the proposed rules and three regulatory analysts.[1421] Finally, the exchange commenter noted that the Commission failed to consider start-up costs associated with complying with reporting requirements.[1422]

In response, the Commission is persuaded by commenters, and is adjusting its estimated staff-review hours and costs that it believes exchanges and market participants will incur to comply with exemption-recognition processes in this Reproposal. These estimates are reflected in the tables below.

Even though the Commission has outlined three different exemption-application processes in this release, the Commission believes that aspects of the processes will become standardized and the data collected for one exemption will be the same as data collected for another exemption. As a result, it is likely that over time some costs will

[1412] CL–CCI–60935 at 7–8 (the same argument applies to proposed §§ 150.10(a)(6) and 150.11(a)(5)). See also CL–Commercial Energy Working Group–60932 at 12 (the same argument applies to proposed § 105.10(a)(6), and § 150.11(a)(5). See also CL–FIA–60937 at 16 (criticism of requirement to produce enhanced information regarding cash market activity and size of cash market exposure.

[1413] CL–ISDA–60931 at 10.

[1414] CL–Commercial Energy Working Group–60932 at 13.

[1415] *Id.*

[1416] CL–ISDA–60931 at 5.

[1417] CL–ICE–60929 at p 17.

[1418] *Id.*

[1419] *Id.*

[1420] *Id.*

[1421] *Id.*

[1422] CL–ICE–60929 at 17.

decrease. Some commenters, however, expressed different views. One commenter stressed that the Commission's proposed exemption processes triggered greater oversight, increased scope of monitoring, and need for additional staff; whereas a standardized application might reduce market-entry barriers.[1423] The same commenter remarked that increased compliance costs and capital investments might lead to decreased market participation and liquidity.[1424] The commenter then suggested the development of a standardized hedge exemption application to minimize monitoring and compliance costs.[1425] Finally, the same commenter asserted that a standardized application might drive efficiency and minimize regulatory risk exposure via innovation.

The Commission continues to believe that there are costs that are not easily quantified. These are qualitative costs that are related to the specific attributes and needs of individual market participants that are hedging. Given that qualitative costs are highly specific, the Commission continues to believe that market participants will choose to incur § 150.9-related costs only if doing so is less costly than complying with position limits and not executing the desired hedge position. Thus, by providing market participants with an option to apply for relief from speculative position limits under reproposed § 150.9, the Commission continues to believe it is offering market participants a way to ease overall compliance costs because it is reasonable to assume that entities will seek recognition of non-enumerated bona fide hedging positions only if the outcome of doing so justifies the costs. This is because the Commission appreciates that the costs of not trading might be substantially higher. The Commission also believes that market participants will consider how the costs of applying for recognition of an non-enumerated bona fide hedging position under reproposed § 150.9 will compare to the costs of requesting a staff interpretive letter under § 140.99, or seeking exemptive relief under CEA section 4a(a)(7). Likewise, exchanges must consider qualitative costs in their decision to create an non-enumerated bona fide hedging position application process or revise an existing program.

[1423] CL–EDF–60944 at 2.

[1424] *Id.*

[1425] *Id.*

The Commission acknowledges that there may also be other costs to market participants if the Commission disagrees with an exchange's decision to recognize an non-enumerated bona fide hedging position under reproposed § 150.9 or under an independent Commission request or review under reproposed § 150.9(d) or (e). These costs will include time and effort spent by market participants associated with a Commission review, which the Commission addresses in the tables below. There also is the possibility that market participants will lose amounts that the Commission can neither predict nor quantify if it became necessary to unwind trades or reduce positions were the Commission to conclude that an exchange's disposition of an non-enumerated bona fide hedging position application is inconsistent with section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1.

A few commenters remarked on this concern and pointed to the term that the Commission would provide applicants a ''commercially reasonable amount of time'' to unwind positions that the Commission determined did not fall within the categories of exempted positions under § 150.9(d)(4), 150.10(d)(4), and 150.11(d)(3).[1426] One commenter explained that if a market participant is required to unwind a position in the middle of its green-lit hedging activity, the unwind could cause ''significant harm to the participant,'' and the ''rapid unanticipated liquidation of positions could result in market disruption''.[1427] The commenter also highlighted that the less-than-24-hours, commercially-reasonable period compels market participants to seek pre-approval of positions by the Commission or not engage in risk mitigation.[1428] The commenter also added that market participants might restrict trading to some exchanges and concentrate market risk on a single exchange.[1429]

[1426] CL–MGEX–90936 at 8; CL–EEI–EPSA–60925 at 10 (one business to unwind is ''unreasonable'' in energy products); CL–NCGA/NGSA–60919 at 13 (concerned about Commission's suggestion that positions can be unwound in less than one business day); CL–NGFA–60941 at 3; CL–NCFC–60930 at 5 (dislikes the one-day unwind period for dairy market).

[1427] CL–MGEX–90936 at 8. *See also* CL–NCGA/NGSA–60919 at 13 (''Unwinding a position quickly in an illiquid market, such as in many non-spot month contracts, could create a significant market disruption.''); CL–NGFA–60941 at 3 (commented that a one-day liquidation ''in thinly traded contracts without broad liquidity'' could be extremely disruptive); CL–NCFC–60930 at 5 (''Requiring the same time period and the same process to unwind the dairy transactions could lead to a market disruption, disorderly trading and regulatory-influence and unnecessary price volatility.'').

The Commission recognizes that costs may result if the Commission disagrees with an exchange's disposition of a non-enumerated bona fide hedging position application under reproposed § 150.9 (or other exempt position under §§ 150.10 or 150.11). The Commission, however, believes such situations will be limited based on the history of exchanges approving similar applications for exemptions to exchange-set limits. Moreover, as explained in the 2016 supplemental proposal, exchanges have incentives to protect market participants from the harms that position limits are intended to prevent, such as manipulation, corners, and squeezes. In addition, an exchange that recognizes a market participant's non-enumerated bona fide hedging position (or other exempt position) that enables the participant to exceed position limits must then deter the same market participant from trading in a manner that causes adverse price impacts on the market; such adverse price impacts may cause financial harm to market participants, or even reputational risk or economic disadvantage to the exchange.[1430]

ix. Costs To Create or Amend Exchange Rules for Non-Enumerated Bona Fide Hedging Position Application Programs

The Commission believes that exchanges electing to process non-enumerated bona fide hedging position applications under reproposed § 150.9(a) are likely to already administer similar processes and will need to file with the Commission amendments to existing exchange rules rather than create new rules. The exchanges will only have to file amendments once. As discussed in the Paperwork Reduction Act discussion below, the Commission forecasts an average annual filing cost of $1,220 per exchange that files new rules or modifications per final process that an exchange adopts. Under the Paperwork Reduction Act, these costs are reported as an average annual cost over a five-year period.

[1428] CL–MGEX–90936 at 8.

[1429] *Id.*

[1430] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38488–89.

TABLE IV–A–6—BURDEN ESTIMATES FOR FILING NEW OR AMENDED RULES

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| New or amended rule filings under part 40 per § 150.9(a)(1), (a)(6) | 6 | 5 | 2 | $122.00 | $1,220 |

x. Costs To Review Applications Under Reproposed Processes

An exchange that elects to process applications also will incur costs related to the review and disposition of such applications pursuant to reproposed § 150.9(a). For example, exchanges will need to expend resources on reviewing and analyzing the facts and circumstances of each application to determine whether the application meets the standards established by the Commission. Exchanges also will need to expend effort in notifying applicants of the exchanges' disposition of recognition or exemption requests. The Commission believes that exchanges electing to process non-enumerated bona fide hedging position applications under reproposed § 150.9(a) are likely to have processes for the review and disposition of such applications currently in place. The Commission has adjusted the costs in Table IV–A–7 based on information submitted by commenters. Thus, the Commission has forecast that the average annual cost for each exchange to process applications for non-enumerated bona fide hedging position recognitions is $277,500.

TABLE IV–A–7—BURDEN ESTIMATES FOR REVIEWING APPLICATIONS

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Collection, review, and disposition of application per § 150.9(a) | 6 | 7 | 325 | $122.00 | $277,550 |

xi. Costs To Post Summaries for Non-Enumerated Bona Fide Hedging Position Recognitions

Exchanges that elect to process the applications under reproposed § 150.9 will incur costs to publish on their Web sites summaries of the unique types of non-enumerated bona fide hedging position positions. The Commission has estimated an average annual cost of $25,620 for the web-posting of non-enumerated bona fide hedging position summaries.

TABLE IV–A–8—BURDEN ESTIMATES FOR POSTING SUMMARIES

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Summaries Posted Online per § 150.9(a) | 6 | 7 | 30 | $122.00 | $25,620 |

xii. Costs To Market Participants Who Will Seek Non-Enumerated Bona Fide Hedging Position Relief From Position Limits

Under reproposed § 150.9(a)(3), market participants must submit applications that provide sufficient information to allow the exchanges to determine, and the Commission to verify, whether it is appropriate to recognize such position as an non-enumerated bona fide hedging position. These applications will be updated annually. Reproposed § 150.9(a)(6) will require applicants to file a report with the exchanges when an applicant owns, holds, or controls a derivative position that has been recognized as an non-enumerated bona fide hedging position. The Commission estimates that each market participant seeking relief from position limits under reproposed § 150.9 will likely incur approximately $976 annually in application costs.[1431]

TABLE IV–A–9—BURDEN ESTIMATES FOR MARKET PARTICIPANTS TO APPLY

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.9(a)(3) Application | 325 | 4 | 2 | $122.00 | $976 |

[1431] Assuming that exchanges administer exemptions to exchange-set limits, these costs are incrementally higher.

xiii. Costs for Non-Enumerated Bona Fide Hedging Position Recordkeeping

The Commission believes that exchanges that currently process applications for spread exemptions and bona fide hedging positions maintain records of such applications as required pursuant to other Commission regulations, including § 1.31. The Commission, however, also believes that the reproposed rules may confer additional recordkeeping obligations on exchanges that elect to process applications for non-enumerated bona fide hedging positions. The Commission estimates that each exchange electing to administer the reproposed non-enumerated bona fide hedging position process will likely incur approximately $3,660 annually to retain records for each process.

TABLE IV–A–10—BURDEN ESTIMATES FOR RECORDKEEPING

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.9(b) Recordkeeping | 6 | 30 | 1 | $122.00 | $3,660 |

xiv. Costs for Weekly and Monthly Non-Enumerated Bona Fide Hedging Position Reporting to the Commission

The Commission anticipates that exchanges that elect to process non-enumerated bona fide hedging position applications will be required to file two types of reports. The Commission is aware that five exchanges currently submit reports each month, on a voluntary basis, which provide information regarding exchange-processed exemptions of all types. The Commission believes that the content of such reports is similar to the information required of the reports in proposed rule § 150.9(c), but the frequency of such required reports will increase under the reproposed rule. The Commission estimates an average cost of approximately $38,064 per exchange for weekly reports under reproposed § 150.9(c).

TABLE IV–A–11—BURDEN ESTIMATES FOR SUBMITTING WEEKLY REPORTS

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.9(c)(1) Weekly Report | 6 | 6 | 52 | $122.00 | $38,064 |

For the monthly report, the Commission anticipates a minor cost for exchanges because the reproposed rules will require exchanges essentially to forward to the Commission notices received from applicants who own, hold, or control the positions that have been recognized or exempted. The Commission estimates an average cost of approximately $8,784 per exchange for monthly reports under reproposed § 150.9(c).

TABLE IV–A–12—BURDEN ESTIMATES FOR SUBMITTING MONTHLY REPORTS

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.9(c)(2) Monthly Report | 6 | 6 | 12 | $122.00 | $8,784 |

xv. Costs Related to Subsequent Monitoring

Exchanges will have additional surveillance costs and duties with respect to non-enumerated bona fide hedging position that the Commission believes will be integrated with their existing self-regulatory organization surveillance activities as an exchange.

b. Section 150.10—Spread Exemptions

Since the Commission issued the June 2016 Supplemental Proposal, the Commission made very few changes to the provisions authorizing exchanges to exempt spread positions from federal position limits under reproposed § 150.10. In addition to non-substantive changes for purposes of clarification, substantive changes were made in subsections s of paragraphs (a) and (c) of § 150.10: §§ 150.10(a)(1)(ii); 150.10(a)(3)(ii) and (iii); 150.10(a)(6); 150.10(c)(2); The Commission did not make changes to paragraphs (b), (d), (e), or (f) of reproposed § 150.10.

i. Section 150.10(a)—Exchange-Administered Spread Exemption

In paragraph (a) of reproposed § 150.10, the Commission identifies the process and information required for an exchange to grant a market participant's request that its derivative position(s) be recognized as an exempt spread position.

As an initial step under reproposed § 150.10(a)(1), exchanges that voluntarily elect to process spread exemption applications are required to notify the Commission of their intention to do so by filing new rules or rule amendments with the Commission under part 40 of the Commission's regulations. The Commission clarified reproposed § 150.10(a)(1)(ii) to explain that an exchange may offer spread exemptions if the contract, which is either a component of the spread or a referenced contract that is related to the spread, in a particular commodity is actively traded. The Commission reduced the burden of proposed § 150.10(a)(1)(ii) (that would require an exchange to have applied position limits for at least one year), by providing in reproposed § 150.10(a)(1) that an exchange must have at least one year of experience and expertise administering position limits for such referenced contract. As explained above, the exchange may gain such experience and expertise, for example, through employing experienced staff.

In reproposed § 150.10(a)(2), the Commission identifies four types of spreads that an exchange may approve. Reproposed § 150.10(a)(3) describes in general terms the type of information that exchanges should collect from applicants. In reproposed § 150.10(a)(3)(ii), similar to the change made in § 150.9(a)(3), the Commission changed the requirement that the application process require an applicant submit ''detailed information'' in regards to certain information to ''information.'' The change provides the exchanges with the discretion to determine what level of detail is needed to make their determination. The Commission clarified the reproposed requirements to explain that applicant must report its maximum size of all gross positions in the commodity related to the spread-exemption application. Reproposed § 150.10(a)(4) obliges applicants and exchanges to act timely in their submissions and notifications, respectively, and require exchanges to retain revocation authority. Reproposed § 150.10(a)(6) was modified and authorizes exchanges to determine whether enhanced reporting is necessary. Reproposed § 150.10(a)(7) requires exchanges to publish on its Web site a summary describing the type of spread position and explaining why it was exempted.

ii. Section 150.10(b)—Spread Exemption Recordkeeping Requirements

The Commission made no changes to the regulatory text in § 150.10(b) that was proposed in June 2016. Under the reproposed rule, exchanges must maintain complete books and records of all activities relating to the processing and disposition of spread exemption applications under reproposed § 150.10(b). This is similar to the record retention obligations of exchanges for positions recognized as non-enumerated bona fide hedging positionss.

iii. Section 150.10(c)—Spread Exemption Reporting Requirements

The Commission amended § 150.10(c)(2) and kept the rest of regulatory text in § 150.10(c) the same as the text proposed in the 2016 supplemental proposal. Under the reproposed rule exchanges will have weekly reporting obligations for spread exemptions. The change in subsection (c)(2) clarifies that exchanges have the discretion to determine whether applicants should have monthly reports that must ultimately be sent to the Commission. These reporting obligations are similar to the reporting obligations of exchanges for positions recognized as non-enumerated bona fide hedging positions.

iv. Baseline

For the reproposed spread exemption process for positions subject to federal limits, the baseline is CEA section 4a(a)(1). In that statutory section, the Commission is authorized to recognize certain spread positions. That statutory provision is currently implemented in a limited calendar-month spread exemption in § 150.3(a)(3). For exchange-set position limits, the baseline for spreads is the guidance in current § 150.5(a), which provides generally that exchanges may recognize exemptions for positions that are normally known to the trade as spreads.

v. Benefits

CEA section 4a(a)(1) authorizes the Commission to exempt certain spreads from speculative position limits. In exercising this authority, the Commission recognizes that spreads can have considerable benefits for market participants and markets. The Commission now proposes a spread exemption framework that utilizes existing exchanges—resources and exchanges—expertise so that fair access and liquidity are promoted at the same time market manipulations, squeezes, corners, and any other conduct that will disrupt markets are deterred and prevented. Building on existing exchange processes preserves the ability of the Commission and exchanges to monitor markets and trading strategies while reducing burdens on exchanges that will administer the process, and market participants, who will utilize the process.

In addition to these benefits, there are other benefits related to reproposed § 150.10 that will inure to markets and market participant. Yet, there is difficulty in quantifying these benefits because benefits are dependent on the characteristics, such as operational size and needs, of the market participants that will seek spread exemptions, and the markets in which the participants trade. Accordingly, the Commission considers the qualitative benefits of reproposed § 150.10.

For both exchanges and market participants, reproposed § 150.10 will likely alleviate compliance burdens to the status quo. Exchanges will be able to build on established procedures and infrastructure. As stated earlier, many exchanges already have rules in place to process and grant applications for spread exemptions from exchange-set position limits pursuant to part 38 of the Commission's regulations (in particular, current § 38.300 and § 38.301) and current § 150.5. In addition, exchanges may be able to use the same staff and electronic resources that will be used for reproposed § 150.9 and § 150.11. Market participants also may benefit from spread-exemption reviews by exchanges that are familiar with the commercial needs and practices of market participants seeking exemptions. Market participants also might gain legal and regulatory clarity and consistency that will help in developing trading strategies. Moreover, the Commission has reduced burdens by making changes to proposed §§ 150.10(a)(1) and (3). In the reproposed § 150.10(a)(1), the Commission changed the rule so that exchanges may employ experienced staff to satisfy the requirement that an exchange have at least one year of experience and expertise in administering position limits for referenced contracts related to spread exemptions. In reproposed § 150.10(a)(3)(ii), the Commission gave exchanges greater discretion in determining the level of detail needed from spread-exemption applicants.

Reproposed § 150.10 will authorize exchanges to approve spread exemptions that permit market participants to continue to enhance liquidity, rather than being restricted by a position limit. For example, by allowing speculators to execute intermarket and intramarket spreads in accordance with reproposed § 150.3(a)(1)(iv) and § 150.10, speculators will be able to hold a greater amount of open interest in underlying contract(s), and, therefore, bona fide hedgers may benefit from any increase in market liquidity. Spread exemptions might lead to better price continuity and price discovery if market participants who seek to provide liquidity (for example, through entry of resting orders for spread trades between different contracts) receive a spread exemption and, thus, will not otherwise be constrained by a position limit.

Here are two examples of positions that could benefit from the spread exemption in reproposed § 150.10:

- Reverse crush spread in soybeans on the CBOT subject to an intermarket spread exemption. In the case where soybeans are processed into two different products, soybean meal and soybean oil, the crush spread is the difference between the combined value of the products and the value of soybeans. There are two actors in this scenario: The speculator and the soybean processor. The spread's value approximates the profit margin from actually crushing (or mashing) soybeans into meal and oil. The soybean processor may want to lock in the spread value as part of its hedging strategy, establishing a long position in soybean futures and short positions in soybean oil futures and soybean meal futures, as substitutes for the processor's expected cash market transactions (purchase of the anticipated inputs for processing and sale of the anticipated products). On the other side of the processor's crush spread, a speculator takes a short position in soybean futures against long positions in soybean meal futures and soybean oil futures. The soybean processor may be able to lock in a higher crush spread, because of liquidity provided by such a speculator who may need to rely upon a spread exemption. It is important to understand that the speculator is accepting basis risk represented by the crush spread, and the speculator is providing liquidity to the soybean processor. The crush spread positions may result in greater correlation between the futures prices of soybeans and those of soybean oil and soybean meal, which means that prices for all three products may move up or down together in a closer manner.

• Wheat spread subject to intermarket spread exemptions. There are two actors in this scenario: The speculator and the wheat farmer. In this example, a farmer growing hard wheat will like to reduce the price risk of her crop by shorting MGEX wheat futures. There, however, may be no hedger, such as a mill, that is immediately available to trade at a desirable price for the farmer. There may be a speculator willing to offer liquidity to the hedger; the speculator may wish to reduce the risk of an outright long position in MGEX wheat futures through establishing a short position in CBOT wheat futures (soft wheat). Such a speculator, who otherwise will have been constrained by a position limit at MGEX or CBOT, may seek exemptions from MGEX and CBOT for an intermarket spread, that is, for a long position in MGEX wheat futures and a short position in CBOT wheat futures of the same maturity. As a result of the exchanges granting an intermarket spread exemption to such a speculator, who otherwise may be constrained by limits, the farmer might be able to transact at a higher price for hard wheat than might have existed absent the intermarket spread exemptions. Under this example, the speculator is accepting basis risk between hard wheat and soft wheat, reducing the risk of a position on one exchange by establishing a position on another exchange, and potentially providing liquidity to a hedger. Further, spread transactions may aid in price discovery regarding the relative protein content for each of the hard and soft wheat contracts.

Finally, the Commission is allowing exchanges to recognize and exempt spreads during the five-day spot month. There may be considerable benefits that evolve from spreads exempted during the spot month, in particular. Besides enhancing the opportunity for market participants to use strategies involving spread trades into the spot month, this relief may improve price discovery in the spot month for market participants. And, as in the intermarket wheat example above, the spread relief in the spot month may better link prices between two markets, *e.g.,* the price of MGEX wheat futures and the price of CBOT wheat futures. Put another way, the prices in two different but related markets for substitute goods may be more highly correlated, which benefits market participants with a price exposure to the underlying protein content in wheat generally, rather than that of a particular commodity.

vi. Costs and Discussion of Comments

As discussed in the 2016 supplemental proposal, the Commission has been able to quantify some costs, but other costs related to reproposed § 150.10 are not easily quantifiable. The Commission continues to believe that some costs are more dependent on individual markets and market participants seeking a spread exemption, and, thus, are more readily considered qualitatively. In general, the Commission believes that reproposed § 150.10 should provide exchanges and market participants greater regulatory and administrative certainty and that costs will be small relative to the benefits of having an additional trading tool under reproposed § 150.10.

The Commission comes to this conclusion even though the most common complaint about the spread-exemption process is that it requires excessive reporting. One exchange commenter focused specifically on the spread-exemption-recognition process, and stated that it is ''overly prescriptive as to the information that must be provided by the applicant, especially when the exchange may have superior information regarding intramarket spreads.'' [1432] The exchange commenter criticized the proposed intramarket spread exemption application as possibly being ''inefficient and time consuming thereby hindering the exchange from effectively supporting its bona fide hedgers.'' [1433] And the exchange commenter suggested that the Commission grant the exchanges the ''flexibility and discretion to establish'' application processes.[1434] The exchange commenter further explained that exchanges are best positioned to assess liquidity for bona fide hedgers and perform the price discovery function for granting exemptions, which, in turn protects market participants and the public.[1435]

The Commission recognizes that spread-exemption application requirements and reporting requirements are detailed. Moreover, these costs will be borne by exchanges and market participants. But, the Commission continues to believe that the qualitative costs will be reasonable in view of the benefits to exchanges and market participants of being able to use spread exemptions. Furthermore, the benefits of having an application process and reporting regime will create cost-savings to the public in the form of enhanced regulatory oversight.

The Commission, however, did respond to comments about proposed § 150.10(a)(3)(iii), which requires an applicant to identify ''the maximum size of all gross positions in derivative contracts to be acquired by the applicant during the year after the application is submitted.'' The comment was that the requirement was too broad and almost impossible because of the inability to predict trading activity over the next year.[1436] Another commenter described the proposed rule as ''unnecessary and unduly burdensome.'' [1437] The Commission, as discussed above regrading reproposed § 150.9(a)(3)(iii), has clarified in reproposed § 150.10(a)(3)(iii) that the filing must include the maximum size of all gross positions for which the application is submitted, which may be a longer time period that the proposed one-year period. As noted above, in administering requests for recognition of non-enumerated bona fide hedging position exemptions under § 1.47, the Commission has found a maximum size statement, as required under § 1.47(b)(4), to be useful both at the time

[1432] CL–Nodal–60948 at 2.

[1433] *Id.*

[1434] *Id.* at 3.

[1435] *Id.* at 4.

[1436] CL–ISDA–60931 at 10.

[1437] CL–Working Group–60947 at 10.

of review of the filing and at the time of review of a filer's position that exceeds the level of the position limit.

Finally, like the discussion about quantified costs related to repproposed § 150.9, exchanges and market participants may have already many of the financial outlays for administering the application process and applying for spread exemptions, respectively. Yet, as commenters have asserted, the Commission might have underestimated the costs. In deference to the comments, the Commission has adjusted its estimates of quantified costs that will arise from repproposed § 150.10 in Tables IV–A–13 through IV–A–19, below. The Commission's new estimates are based on commenters noting that the Commission estimated staff hours, as well as the number of exemption requests, were low.

*Note:* The activities priced in Tables A2 to G2 are similar to the activities discussed in the section affiliated with Tables A1 through G1, above.

TABLE IV–A–13—BURDEN ESTIMATES FILING NEW OR AMENDED RULES

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| New or amended rule filings under part 40 per § 150.10(a)(1), (a)(6) | 6 | 5 | 2 | $122.00 | $1,220 |

TABLE IV–A–14—BURDEN ESTIMATES FOR REVIEWING APPLICATIONS

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Collection, review, and disposition of application per § 150.10(a) | 6 | 7 | 85 | $122.00 | $72,590 |

TABLE IV–A–15—BURDEN ESTIMATES FOR POSTING SUMMARIES

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Summaries Posted Online per § 150.10(a) | 6 | 7 | 10 | $122.00 | $8,540 |

Regarding the following Table D2, note that reports are also required to be sent to the Commission in the case of exempt spread positions under § 150.10(a)(5).

TABLE IV–A–16—BURDEN ESTIMATES FOR MARKET PARTICIPANTS TO APPLY

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.10(a)(3) Spread Exemption Application | 85 | 3 | 2 | $122.00 | $732 |

TABLE IV–A–17—BURDEN ESTIMATES FOR RECORDKEEPING

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.10(b) Recordkeeping | 6 | 30 | 1 | $122.00 | $3,660 |

TABLE IV–A–18—BURDEN ESTIMATES FOR SUBMITTING WEEKLY REPORTS

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.10(c)(1) Weekly Report | 6 | 6 | 52 | $122.00 | $38,064 |

TABLE IV–A–19—BURDEN ESTIMATES FOR SUBMITTING MONTHLY REPORTS

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.10(c)(2) Monthly Report | 6 | 6 | 12 | $122.00 | $8,784 |

Other costs to exchanges will include those related to surveillance. For example, exchanges that elect to grant spread exemptions will have to adapt and develop procedures to determine whether a particular spread exemption furthers the goals of CEA section 4a(a)(3)(B) as well as monitor whether applicant speculators are, in fact, providing liquidity to other market participants. There will likely also be costs related to disagreements between the Commission and exchanges over exchanges' disposition of a spread applications, or costs from a Commission request or review under reproposed § 150.11(d) or (e). As expressed in the 2016 supplemental proposal, these costs are not easily quantified because they depend on the specifics of the Commission's request or review.

c. Section 150.11—Enumerated Anticipatory Bona Fide Hedges

Between the 2016 Supplemental Proposal and now, the Commission is making two changes in the following regulatory text: § 150.11(a)(1)(v) and § 150.11(a)(6).

i. Section 150.11(a)—Exchange-Administered Enumerated Anticipatory Bona Fide Hedge Process

Under reproposed § 150.11(a)(1), exchanges that voluntarily elect to process enumerated anticipatory bona-fide hedge applications are required to notify the Commission of their intention to do so by filing new rules or rule amendments with the Commission under part 40 of the Commission's regulations. In reproposed § 150.11(a)(1)(v), the Commission clarified that exchanges that elect to offer a § 150.11 exemption, must have at least one year of experience and expertise in the referenced contract, rather than the derivative contract. In reproposed § 150.11(a)(2), the Commission identifies certain types of information necessary for the application, including information required under reproposed § 150.7(d). In reproposed § 150.11(a)(3), the Commission states that applications must be updated annually and that the exchanges have ten days in which to recognize an enumerated anticipatory bona fide hedge. In addition, exchanges must retain authority to revoke recognitions. reproposed § 150.11(a)(4) states that once an enumerated anticipatory bona fide hedging position has been recognized by an exchange, the position will be deemed to be recognized by the Commission. Reproposed § 150.11(a)(5) discusses reports that must be filed by an applicant holding an enumerated anticipatory bona fide hedging position, as required under reproposed § 150.7(e). The Commission clarified those reporting requirements, which were also proposed in § 150.11(a)(3)(i), and eliminated language that was confusing to commenters regarding updating and maintaining the accuracy of such reports. Reproposed 150.11(a)(6) explains that exchanges may choose to seek Commission review of an application and the Commission has ten days in which to respond.

ii. Section 150.11(b)—Enumerated Anticipatory Bona Fide Hedge Recordkeeping Requirements

The Commission did not make any changes to § 150.11(b) as proposed in the 2016 supplemental proposal. Exchanges must maintain complete books and records of all activities relating to the processing and disposition of anticipatory hedging applications under reproposed § 150.11(b).

iii. Section 150.11(c)—Enumerated Anticipatory Bona Fide Hedge Reporting Requirements

The Commission did not make any changes to § 150.11(c) as proposed in the 2016 supplemental proposal. Exchanges will have weekly reporting obligations under reproposed § 150.11(c).

iv. Baseline

The baseline is the same as it was in the December 2013 Position Limits Proposal: The current filing process detailed in current § 1.48.

v. Benefits

There are significant benefits that will likely accrue should § 150.11 be finalized. Recognizing anticipatory positions as bona fide hedging positions under § 150.11 will provide market participants with potentially a more expeditious recognition process than the Commission proposal for a 10-day Commission recognition process under reproposed § 150.7. The benefit of prompter recognitions, though, is not readily quantifiable, and, in most circumstances, is subject to the characteristics and needs of markets as well as market participants. So it is challenging to quantify the benefits that will likely be associated with reproposed § 150.11.

For example, exchanges will be able to use existing resources and knowledge in the administration and assessment of enumerated anticipatory bona fide hedging positions. The Commission and exchanges have evaluated these types of positions for years (as discussed in the December 2013 Position Limits Proposal). Utilizing this experience and familiarity will likely produce such benefits as prompt but reasoned decision making and streamlined procedures. In addition, reproposed § 150.11 permits exchanges to act in less than ten days—a timeframe that will be less than the Commission's process under current § 1.48, or under reproposed § 150.7.[1438] This could potentially enable commercial market participants to pursue trading strategies in a more timely fashion to advance their commercial and hedging needs to reduce risk.

Reproposed § 150.11, similar to reproposed § 150.9 and § 150.10, also will provide the benefit of enhanced record-retention and reporting of positions recognized as enumerated anticipatory bona fide hedging positions. As previously discussed, records retained for specified periods will enable exchanges to develop consistent practices and afford the Commission accessible information for review, surveillance, and enforcement efforts. Likewise, weekly reporting under § 150.11 will facilitate the tracking of positions by the Commission.

vi. Costs and Discussion of Comments

The § 150.11-related comments in response to the 2016 supplement proposal's request for comments

[1438] *See* discussion in December 2013 Position Limits Proposal, 78 FR 75745–46, Dec. 12, 2013.

centered on the claim that the exemption process and reporting requirements are burdensome. Nevertheless, as explained above, the Commission made a few changes to clarify application and reporting requirements.

The costs for reproposed § 150.11 are similar to the costs for reproposed §§ 150.9 and 150.10, and have been quantified are in Tables A3 through G3. As mentioned earlier, the Commission has increased the number of staff hours and exemption requests based on commenters stating that the Commission underestimated costs. Other costs associated with reproposed § 150.11, like those for reproposed §§ 150.9 and 150.10, are more qualitative in nature and hinge on specific market and participant attributes. Other costs could arise from reproposed § 150.11 if the Commission disagrees with an exchange's disposition of an enumerated anticipatory bona fide hedging position application, or costs from a Commission request or review under reproposed § 150.11(d). These costs will include time and effort spent by market participants associated with a Commission review. In addition, market participants will lose amounts that the Commission can neither predict nor quantify if it became necessary to unwind trades or reduce positions were the Commission to conclude that an exchange's disposition of an enumerated anticipatory bona fide hedging position application is not appropriate or is inconsistent with the Act. This concern was raised by commenters as discussed above. The Commission believes that such disagreements will be rare based on the Commission's past experience and review of exchanges' efforts. Nevertheless, the Commission notes that assessing whether a position is for the reduction of risk arising from anticipatory needs or excessive speculation is complicated.

**Note:** For a general description of reproposed rules identified in the following Tables IV–A–20 to IV–A–24, see discussion above.

TABLE IV–A–20—BURDEN ESTIMATES FOR FILING NEW OR AMENDED RULES

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| New or amended rule filings under part 40 per § 150.11(a)(1), (a)(5) | 6 | 5 | 2 | $122.00 | $1,220 |

TABLE IV–A–21—BURDEN ESTIMATES FOR REVIEWING APPLICATIONS

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| Collection, review, and disposition of application per § 150.11(a) | 6 | 7 | 90 | $122.00 | $76,860 |

TABLE IV–A–22—BURDEN ESTIMATES FOR MARKET PARTICIPANTS TO APPLY

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.11(a)(2) Application on Form 704 | 90 | 3 | 2 | $122.00 | $732 |

TABLE IV–A–23—BURDEN ESTIMATES FOR RECORDKEEPING

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.11(b) Recordkeeping | 6 | 30 | 1 | $122.00 | $3,660 |

TABLE IV–A–24—BURDEN ESTIMATES FOR SUBMITTING WEEKLY REPORTS

| Required record or report | Total number of respondents | Burden hours per response | Annual number of responses per respondent | Hourly wage estimate | Per-entity labor cost |
|---|---|---|---|---|---|
| § 150.11(c) Weekly Report | 6 | 6 | 52 | $122.00 | $38,064 |

Exchanges will have additional surveillance costs and duties that the Commission believes will be integrated with their existing self-regulatory organization surveillance activities as an exchange.

10. Summary of CEA Section 15(a) Factors

CEA section 15(a) requires the Commission to consider the costs and benefits of its actions in light of five factors.

a. Protection of Market Participants and the Public

The imposition of position limits is intended to protect the markets and market participants from manipulation and excessive speculation. Position limits may serve as a prophylactic measure that reduces market volatility due to a participant otherwise engaging in large trades that induce price impacts. Such price impacts may occur when a party who is holding large open interest is not willing or is unable to meet a call for additional margin. In such an instance, a substantial amount of open interest may have to be liquidated in a short time interval. In addition, price impacts could also occur from a large trader establishing or liquidating large positions.

There are additional benefits to imposing position limits in the spot month. Spot month position limits are designed to deter and prevent corners and squeezes as well as promote a more orderly liquidation process at expiration.[1439] Spot month position limits may also make it more difficult to mark the close of a futures contract to possibly benefit other contracts that settle on the closing futures price. Marking the close harms markets by spoiling convergence between futures prices and spot prices at expiration. Convergence is desirable, because many market participants want to hedge the spot price of a commodity at expiration. In addition, since many other contracts, including cash market contracts, settle based on the futures price at expiration, the mispricing might affect a larger amount of the commodity than the deliverable supply of the futures contract.

The CEA provides that position limits do not apply to positions shown to be bona fide hedging positions, as defined by the Commission, or spread positions, as recognized by the Commission. Exemptions from federal position limits for bona fide hedging positions of qualified market participants help ensure the hedging utility of the futures markets while protecting market participants from excess speculation. The Commission believes that the reproposed rules will preserve the important protections of the federal position limit regime while maintaining the hedging function of the futures or swaps markets.

The Commission believes the exemption provisions of these reproposed rules will have a negligible effect on the protection afforded market participants and the public, as compared to the level of protection that is provided by the exemptions policy reflected currently in § 150.3. Moreover, by expanding current § 150.3 to allow exchanges to review applications for exemptions from federal limits, the Commission will be able to rely on the exchanges' experience and expertise in monitoring their own contract markets, with Commission supervision, to help ensure that any exemptions do not detract from the protection of market participants and the public. Because exchanges have experience and expertise, including as part of their SRO functions, the Commission believes they will be able to carefully design exemptions under which position limits will continue to protect market participants while meeting needs for bona fide hedging. Moreover, exchanges have strong incentives—such as maintaining credibility of their markets through protecting against the harms of excessive speculation and manipulation—to appropriately administer exemptions.

b. Efficiency, Competitiveness, and Financial Integrity of Futures Markets

There is a potential market integrity issue with excess speculation. People may not be willing to participate in a futures market if they perceive that there is a participant with an unusually large speculative position exerting what they believe is unreasonable market power. A lack of participation may harm liquidity, and consequently, may harm market efficiency.

On the other hand, traders who find position limits binding may have to trade in substitute instruments—such as futures contracts that are similar but not the same as the core referenced futures contract, forward contracts, trade options, or futures on a foreign board of trade—in order to meet their demand for speculative instruments. These traders may also decide to not trade beyond the federal speculative position limit. Trading in substitute instruments may be less effective that trading in referenced contracts and, thus, may raise the transaction costs for such traders. In these circumstances, futures prices might not fully reflect all the speculative demand to hold the futures contract, because substitute instruments may not fully influence prices the same way that trading directly in the futures contract does. Thus, market efficiency might be harmed.

c. Price Discovery

Reduced liquidity may have a negative impact on price discovery. In the absence of position limits, market participants might elect to trade less as a result of a perception that the market pricing is unfair as a consequence of what they perceive is the exercise of too much market power by a larger speculator. On the other hand, liquidity may also be harmed by a speculator being restricted from additional trading by a position limit. The Commission has set the levels of position limits at high levels, to avoid harming liquidity that may be provided by speculators that would establish large positions, while restricting speculators from establishing extraordinarily large positions. The Commission believes that the recognition and exemption processes will foster liquidity and potentially improve price discovery by making it easier for market participants to have their bona fide hedging exemptions and spread exemptions recognized, however.

Position limits may serve as a prophylactic measure that reduces market volatility due to a participant otherwise engaging in large trades that induce price impacts which interrupt price discovery. Spot month position limits make it more difficult to mark the close of a futures contract to possibly benefit other contracts that settle on the closing futures price. Marking the close harms markets by spoiling convergence between futures prices and spot prices at expiration and damaging price discovery.

d. Sound Risk Management Practices

The Commission believes that traders knowing their positions and ensuring that they do not exceed a position limit or exempted level is a sound risk management practice. Under the exemption processes, market participants must explain and document the methods behind their hedging or spreading strategies to exchanges, and the Commission or exchanges would have to evaluate them. As a result, the Commission believes that the evaluation processes should help market participants, exchanges, the Commission, and the public to understand better the risk management techniques and objectives of various market participants.

e. Other Public Interest Considerations

The Commission has not identified any other public interest considerations.

[1439] Most futures contracts do not ultimately result in physical delivery. Instead, most positions are eliminated by a trader taking an offsetting position in the contract.

The Commission declined to treat the goal of fostering innovation and growth for the betterment of markets as an additional public interest consideration, because these objectives are amorphous and likely difficult to accomplish with a position limit. Instead, exchanges have proper incentives and a variety of tools, including financial innovation, with which to increase liquidity on their exchanges.

9. CEA Section 15(b) Considerations

Section 15(b) of the CEA requires the Commission to consider the public interest to be protected by the antitrust laws and to endeavor to take the least anticompetitive means of achieving the objectives, policies and purposes of the CEA, before promulgating a regulation under the CEA or issuing certain orders. The Commission believes that the rules and guidance in this notice are consistent with the public interest protected by the antitrust laws.

The Commission acknowledges that, with respect to exchange qualifications to recognize or grant non-enumerated bona fide hedging positions, spread exemptions, and anticipatory bona fide hedging position exemptions for federal position limit purposes, the threshold experience requirements that it is reproposing will advantage certain more-established incumbent DCMs (''incumbent DCMs'') over smaller DCMs seeking to expand or future entrant DCMs (collectively ''entrant DCMs'') or SEFs.[1440] Specifically, incumbent DCMs—based on their past track records of: (1) Listing actively traded referenced contracts or actively traded components of spreads; and (2) setting and administering exchange-set position limits applicable to those contracts for at least a year, or having otherwise hired staff with such position limit experience gained elsewhere—will be immediately eligible to submit rules to the Commission under part 40 of the Commission's regulations to process trader applications for recognition of non-enumerated bona fide hedging positions, spread exemptions,[1441] and anticipatory bona fide hedges; in contrast, entrant DCMs and SEFs will be foreclosed from doing so until such time as they have met the eligibility criteria, although the Commission has clarified in the reproposed rule that any exchange may meet the experience requirement, but not the actively traded contract requirement, by hiring staff with appropriate experience. However, in the absence of any comments supporting a contrary view, the Commission does not perceive that an ability to process applications for non-enumerated bona fide hedging positions, spread exemptions and/or anticipatory bona fide hedging positions is a necessary function for a DCM or SEF to compete effectively as a trading facility. In the event an incumbent DCM declines to process a trader's request for hedging recognition or a spread exemption,[1442] the trader may seek the recognition or exemption directly from the Commission in order to trade on an entrant DCM or SEF. Accordingly, the Commission does not view the reproposed threshold experience requirements as establishing a barrier to entry or competitive restraint likely to facilitate anticompetitive effects in any relevant antitrust market for contract trading.[1443]

The Commission invited comment on any considerations related to the public interest to be protected by the antitrust laws and potential anticompetitive effects of the proposal, as well as data or other information to support such considerations. One exchange commenter responded that it was concerned that the overly prescriptive intramarket spread exemption application process might diminish spread trading on all exchanges.[1444] More specifically, the exchange commenter stated that it believed it would be adversely affected by the proposed spread exemption rule because it is an exchange that offers a certain type of spread trading.[1445] Moreover, the exchange commenter relies on intramarket spread trading to enhance liquidity on less actively traded contracts and believes the publication requirement under § 150.10(a)(7) would have an anti-competitive effect.[1446]

In response, the Commission notes that it has the responsibility to review the record of the exchange in granting spread exemptions. For example, a spread trader, who is a speculator, may amass a large position in a referenced contract and a corresponding large position in a non-referenced contract. Such a speculator has an incentive to mark the close of the core referenced futures contract to benefit their large position in a referenced contract. The Commission is concerned that it has an adequate record to review timely a grant of a spread exemption, which would allow a speculator to build a large position in a referenced contract, exempt from position limits. Regarding the publication requirement, the Commission reiterates that the publication requirement is only for a summary describing the type of spread position and why it was exempted and, thus, does not require details of all components of spread trading within low liquidity non-referenced contract markets to be revealed; the Commission notes it would not expect such a summary would reveal identifying information for any trader, but, rather, would reveal, at a minimum, the referenced contract and a generic description of the type of non-referenced contract that is a component of the spread. In addition, the Commission notes that spread trades may qualify as bona fide hedging positions, obviating the need for a spread exemption. Finally, the Commission notes an exchange may petition the Commission for an exemption under CEA section 4a(a)(7) or the Commission staff for a no-action letter under § 140.99.

*B. Paperwork Reduction Act*

1. Overview

The Paperwork Reduction Act (''PRA''), 44 U.S.C. 3501 *et seq.,* imposes certain requirements on Federal agencies, including the Commission, in connection with their conducting or sponsoring any collection of information as defined by the PRA. 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 issued by the Office of Management and Budget (''OMB''). This reproposed rulemaking would result in the collection of information within the meaning of the PRA, as discussed

[1440] *See* reproposed §§ 150.9(a)(1), 150.10(a)(1), and 150.11(a)(1).

[1441] In the case of qualifications to exempt certain spread positions, the contract may be either a referenced contract that is a component of the spread or another contract that is a component of the spread. *See* reproposed § 150.10(a)(1)(i).

[1442] The Commission recognizes that in certain circumstances it might be in an exchange's economic interest to deny processing a particular trader's application for hedge recognition or a spread exemption. For example, this might occur in a circumstance in which a trader has reached the exchange-set limit and the exchange determines that liquidity is insufficient to maintain a fair and orderly contract market if the trader's position increases.

[1443] *See, e.g., Brown Shoe Co.* v. *U.S.,* 370 U.S. 294, 324–25 (1962) (''The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and the substitutes for it''); *U.S.* v. *E.I. du Pont de Nemours & Co.,* 353 U.S. 586, 593 (1957)(''Determination of the relevant market is a necessary predicate to finding a violation''); *Rebel Oil* v. *Atl. Richfield Co.,* 51 F. 3d 1421, 1434 (9th Cir. 1995) (''A 'market' is any grouping of sales whose sellers, if unified by a monopolist or a hypothetical cartel will have market power in dealing with any group of buyers,'' quoting Phillip Areeda & Herbert Hovenkamp, *Antitrust Law* ¶518.1b, at 534 (Supp. 1993)).

[1444] CL–Nodal–60948 at 4.

[1445] *Id.* at 4.

[1446] *Id.* at 4.

below. Specifically, if adopted, it would amend previously-approved collection of information requirements. Therefore, the Commission is submitting this reproposal to OMB for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The information collection requirements reproposed herein will be an amendment to the previously-approved collection associated with OMB control number 3038–0013.[1447]

If the reproposed changes to regulations are adopted, responses to this collection of information would be mandatory. Several of the reporting requirements would be mandatory in order to obtain exemptive relief, and, therefore, would be mandatory under the PRA to the extent a market participant elects to seek such relief. The Commission will protect any proprietary information received in accordance with the Freedom of Information Act and 17 CFR part 145, titled ''Commission Records and Information.'' In addition, the Commission emphasizes that section 8(a)(1) of the Act strictly prohibits the Commission, unless specifically authorized by the Act, from making public ''data and information that would separately disclose the business transactions or market positions of any person and trade secrets or names of customers.'' [1448] The Commission also is required to protect certain information contained in a government system of records pursuant to the Privacy Act of 1974.[1449]

In December 2013, the Commission proposed a number of modifications to its speculative position limits regime. Under that proposal, market participants with positions in a ''referenced contract,'' as defined in § 150.1, would be subject to the position limit framework established in parts 19 and 150 of the Commission's regulations. Proposed changes to part 19 would prescribe new forms and reporting requirements for persons claiming exemptions to speculative position limits and update reporting obligations and required information on existing forms. In proposed part 150, the Commission changed reporting requirements for DCMs listing a core referenced futures contract as well as for traders who wish to apply for an exemption from exchange-set position limits. The Commission also proposed to update and change recordkeeping requirements for market participants and exchanges.

In June 2016, the Commission published in the **Federal Register** a supplemental notice of proposed rulemaking to update and revise the regulations proposed in the December 2013 Position Limits Proposal. The Commission proposed to allow a participant to exceed speculative position limits to the extent that the participant's position is recognized as a non-enumerated bona fide hedging position, an exempt spread position, or an enumerated anticipatory bona fide hedge, by a DCM or SEF. The Commission proposed to require new or amended rule filings under part 40 of its regulations that comply with certain conditions set forth in the revisions to part 150. Further, the proposed changes stated that in order to seek exemptive relief market participants would need to file applications with a DCM or SEF that met criteria established under the proposal.

In this Reproposal, the Commission is reproposing its changes to parts 1, 15, 17, 19, 37, 38, 140, 150, and 151 of the Commission's regulations. Specifically, with regard to the PRA, the Commission is reproposing the following: New and amended series '04 forms under part 19 and § 150.7; submission of deliverable supply estimates under § 150.2(a)(3); recordkeeping obligations under § 150.3(g); revised special call authority under § 150.3(h); exchange set limit exemption application requirements under § 150.5(a)(2); and requirements for recognition of non-enumerated bona fide hedging positions, certain spread positions, and enumerated anticipatory bona fide hedging positions under § 150.9, § 150.10, and § 150.11, respectively.

The Commission proposes reorganizing the information found in the OMB Collection Numbers associated with this rule. In particular, the Commission proposes that the burdens related to series '04 forms be moved from OMB Collection #3038–0009 to OMB Collection #3038–0013. This change is non-substantive but allows for all information collections related to exemptions from speculative position limits to be housed in one collection, making it simpler for market participants to know where to find the relevant PRA burdens. If adopted, OMB Collection #3038–0009 would hold collections of information related to parts 15, 17, and 21 while OMB Collection #3038–0013 would hold collections of information related to parts 19 and 150.

2. Methodology and Assumptions

It is not possible at this time to accurately determine the number of respondents that will be affected by the these rules. Many of the regulations that impose PRA burdens are exemptions that a market participant may elect to take advantage of, meaning that without intimate knowledge of the day-to-day business decisions of all its market participants, the Commission could not know which participants, or how many, may elect to obtain such an exemption. Further, the Commission is unsure of how many participants not currently in the market may be required to or may elect to incur the estimated burdens in the future.

The provisions under § 150.9–11 permits designated contract markets and swap execution facilities to elect to process applications for recognition of non-enumerated bona fide hedging positions, exempt spread positions, or enumerated anticipatory bona fide hedges; accordingly the Commission does not know which, or how many, designated contract markets and swap execution facilities may elect to offer such recognition processes, or which, or how many market participants may submit applications. The Commission is unsure of how many designated contract markets, swap execution facilities, and market participants not currently active in the market may elect to incur the estimated burdens in the future.

Finally, many of the regulations proposed herein are applying to participants in swaps markets for the first time, and the Commission's lack of experience enforcing speculative position limits for such markets and for many of the participants therein hinders its ability to determine with precision the number of affected entities. These limitations notwithstanding, the Commission has made best-effort estimations regarding the likely number of affected entities for the purposes of calculating burdens under the PRA.

3. Information Provided by Reporting Entities/Persons

To determine the number of entities who may file series '04 forms with the Commission and/or exemption applications with DCMs that elect to process such applications, the Commission used its proprietary data collected from market participants as well as information provided by DCMs regarding the number of exemptions processed by exchange surveillance programs each year.[1450] As discussed

[1447] Part 19—Reports by persons holding bona fide hedge positions—currently covered by OMB control number 3038–0009, is being proposed for inclusion in OMB control number 3038–0013.

[1448] 7 U.S.C. 12(a)(1).

[1449] 5 U.S.C. 552a.

[1450] The Commission also described this information in the 2016 Supplemental Position *supra,*[1451] the Commission analyzed data covering a two-year period of July 1, 2014–June 30, 2016 to determine how many participants would have been over 60, 80, 100, 125, 150, 175, 200, and 500 percent of the limit levels in each of the 25 commodities subject to limits under § 150.2 had such levels been in effect during the covered period.[1452] The Commission determined that in that period, 409 unique entities would have exceeded any of the limits in any commodities; the Commission is using a figure of 425 entities to account for any additional entities which may be required to comply with limits. The Commission assumes that only entities over such levels—or close to being over such levels—will file the necessary forms and applications. The Commission's analysis does not account for persons holding hedging or other exemptions from position limits, and the figures provided by DCMs account for exemptions filed for all commodities, not just the 25 subject to limits under § 150.2. Accordingly, the Commission believes the estimates of the number of 425 respondents used herein are highly conservative.

To determine the number of exchanges who would be affected by the reproposal, the Commission analyzed how many exchanges currently list actively traded contracts in the commodities for which federal position limits will be set, as the proposed rules in § 150.5 as well as in §§ 150.9, 150.10, and 150.11 will all apply to exchanges that list commodity derivative contracts that may be subject federal limits under § 150.2(d).

The Commission's estimates concerning wage rates are based on 2013 salary information for the securities industry compiled by the Securities Industry and Financial Markets Association (''SIFMA''). The Commission is using a figure of $122 per hour, which is derived from a weighted average of salaries across different professions from the SIFMA Report on Management & Professional Earnings in the Securities Industry 2013, modified to account for an 1800-hour work-year, adjusted to account for the cumulative rate of inflation since 2013. This figure was then multiplied by 1.33 to account for benefits, and further by 1.5 to account for overhead and administrative expenses. The Commission anticipates that compliance with the provisions would require the work of an information technology professional; a compliance manager; an accounting professional; and an associate general counsel. Thus, the wage rate is a weighted national average of salary for professionals with the following titles (and their relative weight); ''programmer (average of senior and non-senior)'' (15% weight), ''senior accountant'' (15%) ''compliance manager'' (30%), and ''assistant/associate general counsel'' (40%). All monetary estimates below have been rounded to the dollar.

A commenter estimated that for an exchange to promulgate the regulations required of them under this part such an exchange would need a senior level regulation employee and three regulatory analysts.[1453] When the Commission estimated a per-hour wage rate using these professions, however, the average hourly wage rate was lower than the $122 estimated above.[1454] In this reproposal, the Commission is therefore estimating all burdens with the higher wage rate. The Commission notes that the wage rate used for PRA calculations is an average rate, and that some entities may face a higher or lower wage rate based on individual circumstances.

4. Collections of Information

(a) Recordkeeping and Reporting Obligations for Market Participants

(i) Forms 204 and 304

Previously, the Commission estimated the combined annual labor hours for both Form 204 and Form 304 to be 1,350 hours, which amounted to a total labor cost to industry of $68,850 per annum.[1455] Below, the Commission has estimated the costs for each form separately.

As proposed, Form 204 would be required to be filed when a trader accumulates a net long or short commodity derivative position that exceeds a federal limit in a referenced contract. Form 204 would inform the Commission of the trader's cash positions underlying those commodity derivative contracts for purposes of claiming bona fide hedging exemptions.

The Commission estimates that approximately 425 traders would be required to file Form 204 once a month (12 times per year) each. At an estimated 3 labor hours to complete and file each Form 204 report for a total annual burden to industry of 15,300 labor hours, the Form 204 reporting requirement would cost industry $1,866,600 in labor costs.

As proposed, Form 304 would be required to be filed by merchants and dealers in cotton and contains information on the quantity of call cotton bought or sold on a weekly basis. Form 304 would be required in order for the Commission to produce its weekly cotton ''on call'' report.[1456]

The Commission estimates that approximately 200 traders would be required to make a Form 304 submission for call cotton 52 times per year each. At 1 hour to complete each submission for a total annual burden to industry of 10,400 labor hours, the Form 304 reporting requirement would impose upon industry $1,268,800 in labor costs.

(ii) Form 504

As proposed, § 19.01(a)(1) would require persons claiming a conditional spot month limit exemption pursuant to § 150.3(c) to file Form 504. Unlike other series '04 forms, Form 504 would apply only to commodity derivative contracts in natural gas markets.[1457] A Form 504 filing would show the composition of the natural gas cash position underlying a referenced contract that is held or controlled for which the exemption is claimed. The Commission notes that this form should be submitted daily for each day of the 3-day spot period for the core referenced futures contract in natural gas. The Commission estimates that approximately 40 traders would claim a conditional spot month limit 12 times per year, and each corresponding submission would take 15 labor hours to complete and file. Therefore, the Commission estimates that the proposed Form 504 reporting requirement would result in approximately 7,200 total annual labor hours for an additional industry-wide labor cost of $878,400.

Limits Proposal. *See* 2016 Supplemental Position Limits Proposal, 81 FR 38500.

[1451] *See supra* discussion of number of traders over the limit levels.

[1452] The Commission also used this analysis to determine the number of entities subject to the Commission's recordkeeping and special call rules in § 150.3.

[1453] CL–ICE–60929 at 17.

[1454] The Commission computed the alternative wage rate as a weighted national average of salary for professionals with the following titles (and their relative weight); ''compliance manager'' (25 percent weight), 3 ''compliance examiner, intermediate'' (15 percent each) and ''assistant/associate general counsel'' (30 percent). After adjusting for inflation, overhead, and benefits, the wage rate was $107. These titles appeared to best represent the commenter's suggestion but without additional input from the commenter it is impossible to ascertain the commenter's original intent regarding titles of necessary staffing.

[1455] This estimate was based upon an average wage rate of $51 per hour. Adjusted to the hourly wage rate used for purposes of this PRA estimate, the previous total labor cost would have been $202,500.

[1456] The Commission's Weekly Cotton On-Call Report can be found here: *http://www.cftc.gov/MarketReports/CottonOnCall/index.htm.*

[1457] *See supra,* discussion of conditional spot month limit exemption (§ 150.3(c)).

The Commission requests comment on its estimates regarding new Form 504.

(iii) Form 604

Persons claiming a pass-through swap exemption pursuant to § 150.3(a) would be required to file proposed Form 604 showing various data (depending on whether the offset is for non-referenced contract swaps or spot-month swaps) including, at a minimum, the underlying commodity or commodity reference price, the applicable clearing identifiers, the notional quantity, the gross long or short position in terms of futures-equivalents in the core referenced futures contracts, and the gross long or short positions in the referenced contract for the offsetting risk position. For proposed Form 604 reports filed for positions held outside of the spot month, the Commission estimates that approximately 250 traders would claim a pass-through swap exemption an average of 10 times per year each. At approximately 30 labor hours to complete each corresponding submission for a total burden to traders of 75,000 annual labor hours, compliance with the proposed Form 604 filing requirements industry-wide would impose an additional $9,150,000 in labor costs.

(iv) Form 704

Traders claiming anticipatory bona fide hedging exemptions would be required to file proposed Form 704 for the initial statement/application pursuant to § 150.7(d), along with an annual update on the same form. Because annual update requires mostly the same information as the initial statement, allowing market participants to update only fields that have changed since the initial statement was filed rather than having to update the entire form, the Commission anticipates the annual update requiring about half the time to complete. The Commission estimates that approximately 250 traders would claim anticipatory exemptions by filing an initial statement approximately once per year. At an estimated 15 labor hours to complete and file an initial statement on Form 704 for a total annual burden to traders of 3,750 labor hours, the anticipatory exemption filing requirement would cost industry an additional $457,500 in labor costs. The annual update to proposed Form 704 is estimated to be required of the same 250 traders once a year, at an estimated 8 hours to complete and file, for an industry-wide burden of 2,000 hours and $244,000 in labor costs.

(v) Recordkeeping and Other Provisions

Any person claiming an exemption from federal position limits under part 150 would be required to keep and maintain books and records concerning all details of their related cash, forward, futures, options and swap positions and transactions to serve as a reasonable basis to demonstrate reduction of risk on each day that the exemption was claimed. These records would be required to be comprehensive, in that they must cover anticipated requirements, production and royalties, contracts for services, cash commodity products and by-products, pass-through swaps, cross-commodity hedges, and more.

The Commission estimates that approximately 425 traders would claim an average of 50 exemptions each per year that fall within the scope of the recordkeeping requirements of proposed § 150.3(g). At approximately one hour per exemption claimed to keep and maintain the required books and records, the Commission estimates that industry would incur a total of 20,000 annual labor hours amounting to $2,592,500 in additional labor costs.

In addition, proposed § 150.3(h) would provide that upon call from the Commission any person claiming an exemption from speculative position limits under proposed § 150.3 must provide to the Commission any information as specified in the call. It is difficult to determine in advance of any such call who may be required to submit information under proposed § 150.3(h), how that information may be submitted, or how many labor hours it may take to prepare and submit such information. However, for the purposes of the PRA, the Commission has made estimates regarding the potential burden.

The Commission estimates that approximately 425 traders would be eligible to be called upon for additional information under proposed § 150.3(h) each year. At approximately two hours per exemption claimed to keep and maintain the required books and records, the Commission estimates that industry would incur a total of 850 annual labor hours amounting to $103,700 in additional labor costs.

(vi) Exchange-Set Limits and Exchange-Recognized Exemptions

Traders who wish to avail themselves of any exemption from a DCM or SEF's speculative position limit rules would need to submit an application to the DCM or SEF explaining how the exemption would be in accord with sound commercial practices and would allow for a position that could be liquidated in an orderly fashion. As noted supra, the Commission understands that requiring traders to apply for exemptive relief comports with existing DCM practice; thus, the Commission anticipates that the proposed codification of this requirement would have the practical effect of incrementally increasing, rather than creating, the burden of applying for such exemptive relief. The Commission estimates that approximately 425 traders would claim exemptions from DCM or SEF-established speculative position limits each year, with each trader on average making 1 application to the DCM or SEF each year. Each submission is estimated to take 2 hours to complete and file, meaning that these traders collectively would incur a total burden of 850 labor hours per year for an industry-wide additional labor cost of $39,976.

Under proposed §§ 150.9(a)(3), 150.10(a)(3), and 150.11(a)(2), designated contract markets and swap execution facilities that elect to process applications to establish an application process that elicits sufficient information to allow the designated contract market or swap execution facility to determine, and the Commission to verify, whether it is appropriate to recognize a commodity derivative position as an non-enumerated bona fide hedging position, exempt spread position or enumerated anticipatory bona fide hedge, respectively. Pursuant to proposed §§ 150.9(a)(4)(i), 150.10(a)(4), and 150.11(a)(3), an applicant would be required to update an application at least on an annual basis. Further, DCMs and SEFs have authority under §§ 150.9(a)(6), 150.10(a)(6), and 150.11(a)(5) to require that any such applicant file a report with the designated contract market or swap execution facility pertaining to the use of any exemption that has been granted.

The Commission anticipates that market participants would be mostly familiar with the non-enumerated bona fide hedging position application provided by exchanges that currently process such applications, and thus believes that the burden for applying to an exchange would be minimal. Information included in the application would be required to be sufficient to allow the exchange to determine, and the Commission to verify, whether the position meets the requirements of CEA section 4a(c), but specific data fields are left to the exchanges to determine. The Commission notes that there would be a slight additional burden for market participants to submit the notice regarding the use of any exemption granted, should the DCM or SEF require such a report.

The Commission estimates that 325 entities would file an average of 2 applications each year to obtain recognition of certain positions as non-enumerated bona fide hedges and that each application, including any usage report that may be required by the DCM or SEF, would require approximately 4 burden hours to complete and file. Thus, the Commission estimates an average per entity burden of 8 labor hours and an industry-wide burden of 2,600 labor hours annually. The Commission estimates an average cost of approximately $976 per entity or $317,200 for the industry as a whole for applications under § 150.9(a)(3).

The Commission anticipates that market participants would be mostly familiar with the spread exemption application provided by exchanges that currently process such applications, and thus believes that the burden for applying to an exchange would be minimal. Information included in the application is required to be sufficient to allow the exchange to determine, and the Commission to verify, whether the position fulfills the objectives of CEA section 4a(a)(3)(B), but specific data fields are left to the exchanges to determine. The Commission notes that there would be a slight additional burden for market participants to submit the notice regarding the use of any exemption granted should the DCM or SEF require such a report.

The Commission estimates that 85 entities would file an average of 2 applications each year to obtain an exemption for certain spread positions and that each application, including any usage report required by the DCM or SEF, would require approximately 3 burden hours to complete and file. Thus, the Commission approximates an average per entity burden of 6 labor hours and an industry-wide burden of 510 labor hours annually. The Commission estimates an average cost of approximately $732 per entity or $62,220 for the industry as a whole for applications under § 150.10(a)(2).

The Commission anticipates that market participants would be mostly familiar with the enumerated anticipatory bona fide hedge application provided by exchanges that currently process such applications, and thus believes that the burden for applying to an exchange would be minimal. The application is required to include, at a minimum, the information required under § 150.7(d). The Commission estimates that 90 entities would file an average of 2 applications each year to obtain recognition that certain positions are enumerated anticipatory bona fide hedges and that each application would require approximately 3 burden hours to complete and file. Thus, the Commission estimates an average per entity burden of 6 labor hours and an industry-wide burden of 510 labor hours annually. The Commission estimates an average cost of approximately $732 per entity or $65,880 for the industry as a whole for applications under proposed § 150.11(a)(2). The Commission invites comments on any these proposed estimates.

(b) Recordkeeping and Reporting Obligations for DCMs and SEFs

(i) Submission of Estimates of Deliverable Supply

For purposes of assisting the Commission in resetting spot-month limits, proposed § 150.2(e)(3)(ii) would require DCMs to supply the Commission with an estimated spot-month deliverable supply for each core referenced futures contract listed. The estimate must include documentation as to the methodology used in deriving the estimate, including a description and any statistical data employed. The Commission estimates that the submission would require a labor burden of approximately 20 hours per estimate. Thus, a DCM that submits one estimate may incur a burden of 20 hours for a cost of approximately $2,440. DCMs that submit more than one estimate may multiply this per-estimate burden by the number of estimates submitted to obtain an approximate total burden for all submissions, subject to any efficiencies and economies of scale that may result from submitting multiple estimates.

The Commission notes that, in response to comments, the Commission proposes to allow a DCM that does not wish a spot-month limit level to be changed to petition the Commission to not change the limit level and, if the petition is approved, the DCM would not need to submit deliverable supply estimates for such a commodity. A DCM that submits one petition may incur a burden of one hour, resulting in an estimated per-petition cost of approximately $488. Again, DCMs that submit more than one petition may multiply this per-petition burden by the number of petitions submitted.

(ii) Filing New or Amended Rules Pursuant to Part 40

Designated contract markets and swap execution facilities that elect to process the recognition of non-enumerated bona fide hedging positions, exempt spread positions, or enumerated anticipatory bona fide hedging positions would be required to file new rules or rule amendments pursuant to Part 40 of this chapter, establishing or amending its application process for recognition of the above-referenced positions, consistent with the requirements of proposed §§ 150.9, 150.10, and 150.11.

The Commission estimates that, at most, 6 entities would file new rules or rule amendments pursuant to Part 40 to elect to process non-enumerated bona fide hedging, spread, or enumerated anticipatory hedging applications. The Commission determined this estimate by analyzing how many exchanges currently list actively traded contracts for the 28 commodities for which federal position limits would be set, because proposed §§ 150.9(a), 150.10(a), and 150.11(a) would require a referenced contract to be listed by and actively traded on any exchange that elects to process applications for recognition of positions in such referenced contract. The Commission anticipates that the exchanges that would elect to process applications under these sections are likely to have processes for recognizing such exemptions currently, and so would need to file amendments to existing exchange rules rather than adopt new rules. Thus, the Commission approximates an average per entity burden of 10 labor hours.[1458] The Commission estimates an average cost of approximately $1,220 per entity for filing revised rules under part 40 of the Commission's regulations.

(iii) Review and Disposition of Applications

An exchange that elects to process applications may incur a burden related to the review and disposition of such applications pursuant to proposed §§ 150.9(a), 150.10(a), and 150.11(a). The review of an application would be required to include analysis of the facts and circumstances of such application to determine whether the application meets the standards established by the Commission. Exchanges would be required to notify the applicant regarding the disposition of the application, including whether the application was approved, denied, referred to the Commission, or requires additional information.

In the 2016 Supplemental Proposal, the Commission noted that the exchanges that would elect to process non-enumerated bona fide hedging position, exempt spread position, and

[1458] Table IV–B–1 at the end of this section provides a more detailed breakdown of costs.

enumerated anticipatory bona fide hedging position applications are likely to have processes for the review and disposition of such applications currently in place. The Commission noted its preliminary belief that in such cases, complying with the rules would be less burdensome because the exchange would already have staff, policies, and procedures established to accomplish its duties under the rules.

One exchange submitted a comment requesting the Commission alter its estimates of the burdens to exchanges for reviewing such submissions, noting that the proposed rules ''provide[d] for the collection of considerably more documents than are currently required for Exchange exemption requests.'' The commenter continued that the ''review and consideration of these documents will result in additional time spent on each exemption request'' and suggested the Commission increase its estimate from five hours to seven hours per review.[1459] The commenter also suggested the Commission increase the number of applications that exchanges are estimated to process, stating that the Commission's estimate of 285 exemption requests (for all three types of applications) paled in comparison to the exchange's estimate of 500 applications.[1460]

The Commission notes that it is unclear whether the exchange's estimate of 500 applications includes applications in commodities outside of the commodities subject to the proposed rules. If so, the exchange may have overestimated the number of new applications the exchange may process per year. Further, the estimates of one exchange may not be representative of the number of applications received by the other five exchanges. However, in an abundance of caution, the Commission proposes to use the exchange's estimate for the number of applications. Since the commenter did not suggest the proportion of applications was improperly distributed amongst the sections regarding non-enumerated bona fide hedging positions, exempt spread positions, and enumerated anticipatory hedging positions, the Commission has estimated the costs resulting from each type of application using roughly the same proportion as originally proposed.

Thus, the Commission estimates that each exchange would process approximately 325 non-enumerated bona fide hedging position applications per year and that each application would require 7 hours to process, for an average per entity burden of 2,275 labor hours annually. The Commission estimates an average cost of approximately $277,500 per entity under § 150.9(a).

The Commission estimates that each exchange would process about 85 spread exemption applications per year and that each application would require 7 hours to process, for an average per entity burden of 595 labor hours annually. The Commission estimates an average cost of approximately $72,590 per entity under proposed § 150.10(a). The Commission invites comments on these estimates.

The Commission estimates that each entity would process about 90 anticipatory hedging applications per year and that each application would require 7 hours to process, for an average per entity burden of 630 labor hours annually. The Commission estimates an average cost of approximately $76,860 per entity under proposed § 150.11(a).

(iv) Publication of Summaries

Exchanges that would elect to process the applications under proposed §§ 150.9 and 150.10 may incur burdens to publish on their Web sites summaries of the unique types of non-enumerated bona fide hedging position positions and spread positions, respectively. This requirement would be new even for exchanges that already have a similar process under exchange-set limits.

The Commission estimated in the 2016 Supplemental Position Limits Proposal that a single summary would require 5 hours to write, approve, and post. An exchange also commented that these summaries would likely require seven hours per summary to prepare.[1461] Thus, the Commission now estimates that each exchange would post approximately 40 summaries per year, with an average per summary burden of 7 labor hours.[1462] The Commission estimates an average cost of approximately $34,160 per entity, representing the combined burdens of § 150.9(a)(7) and § 150.10(a)(7). The Commission invites comments on these estimates.

(v) Recordkeeping

Designated contract markets and swap execution facilities that elect to process applications are required under proposed §§ 150.9(b), 150.10(b), and 150.11(b) to keep full, complete, and systematic records, which include all pertinent data and memoranda, of all activities relating to the processing and disposition of applications for recognition of non-enumerated bona fide hedging positions, exempt spread positions, and enumerated anticipatory bona fide hedges. The Commission believes that exchanges currently process applications for recognition of non-enumerated bona fide hedging positions, exempt spread positions, and enumerated anticipatory bona fide hedges maintain records of such applications as required pursuant to other Commission regulations, including § 1.31. However, the Commission also believes that the rules may confer additional recordkeeping obligations on exchanges that elect to process applications for recognition of non-enumerated bona fide hedging positions, exempt spread positions, and enumerated anticipatory bona fide hedges.

The Commission estimates that 6 entities would have recordkeeping obligations pursuant to proposed §§ 150.9(b), 150.10(b), and 150.11(b). Thus, the Commission approximates an average per entity burden of 90 labor hours annually for all three sections. The Commission estimates an average cost of approximately $10,980 per entity for records and filings under §§ 150.9(b), 150.10(b), and 150.11(b).[1463] The Commission invites comments on its estimates.

(vi) Reporting

The Commission anticipates that exchanges that elect to process applications for recognition of non-enumerated bona fide hedging positions, spread exemptions, and enumerated anticipatory bona fide hedges would be required to file two types of reports. In particular, proposed §§ 150.9(c) and 150.10(c) would require a designated contract market or swap execution facility that elects to process applications for non-enumerated bona fide hedging positions and exempt spread positions to submit to the Commission (i) a summary of any non-enumerated bona fide hedging position and exempt spread position newly published on the designated contract market or swap execution facility's Web site; and (ii) no less frequently than monthly, any report submitted by an applicant to such designated contract market or swap execution facility pursuant to rules authorized under

[1459] *See* CL–ICE–60929 at 17.

[1460] *Id.*

[1461] *See* CL–ICE–60929 at 17.

[1462] The Commission has combined the burdens for summaries published in accordance with § 150.9(a)(7) and § 150.10(a)(7) in order to make the text clearer. Table IV–B–1 at the end of this section provides a more detailed breakdown of costs by regulation.

[1463] The Commission has combined the burdens for recordkeeping under §§ 150.9(b), 150.10(b), and 150.11(b). Table IV–B–1 at the end of this section provides a more detailed breakdown of costs by regulation.

proposed §§ 150.9(a)(6)and 150.10(a)(6), respectively. Further, proposed §§ 150.9(c), 150.10(c), and 150.11(c) would require designated contract markets and swap execution facilities that elect to process relevant applications to submit to the Commission a report for each week as of the close of business on Friday showing various information concerning the derivative positions that have been recognized by the designated contract market or swap execution facility as an non-enumerated bona fide hedging position, exempt spread position, or enumerated anticipatory bona fide hedge position, and for any revocation, modification or rejection of such recognition.

The Commission understands that 5 exchanges currently submit reports, on a voluntary basis each month, which provide information regarding exchange-recognized exemptions of all types. The Commission stated in the 2016 Supplemental Position Limits Proposal its preliminary belief that the content of such reports is similar to the information required of the reports in §§ 150.9(c), 150.10(c), and 150.11(c), but the frequency of such reports would increase under the proposed rules. The Commission estimated that the weekly report would require approximately 3 hours to complete and submit and that the monthly report would require 2 hours to complete and submit.

An exchange commented that the Commission ''significantly understated'' the time required to prepare, review, and submit the weekly and monthly reports based on the amount of time the exchange currently spends to prepare and submit the reports it already submits. The commenter suggested the Commission revise its estimates to reflect the exchange's estimates of six hours to prepare the weekly report and six hours to prepare the monthly report.[1464]

The Commission estimates that 6 entities would have weekly reporting obligations pursuant to reproposed §§ 150.9(c)(1), 150.10(c)(1), and 150.11(c).[1465] The Commission is revising its estimate to reflect the commenter's assertion that the weekly report will require a burden of approximately 6 hours to complete and submit. Thus, the Commission estimates an average per entity burden of 936 labor hours annually. The Commission estimates an average cost of approximately $114,192 per entity for weekly reports pursuant to all three related sections. The Commission invites comments on its estimates.

The Commission also estimates that 6 entities would have monthly reporting obligations pursuant to reproposed §§ 150.9(c)(2) and 150.10(c)(2).[1466] The Commission also estimates that the monthly report would require a burden of approximately 6 hours to complete and submit. Thus, the Commission approximates an average per entity burden of 144 labor hours annually. The Commission estimates an average cost of approximately $17,568 per entity for monthly reports under both sections.

TABLE IV–B–1—BREAKDOWN OF BURDEN ESTIMATES BY REGULATION AND TYPE OF RESPONDENT

| Type of respondent<br>A | Required record or report<br>B | Total number of respondents<br>C | Annual number of responses per respondent<br>D | Total annual responses<br>E [1467] | Estimated number of burden hours per response<br>F | Annual burden<br>G [1468] |
|---|---|---|---|---|---|---|
| Exchange .. | New or amended rule filings under part 40 per § 150.9(a)(1), (a)(6). | 6 | 2 | 12 | 5 | 60 |
| Exchange .. | New or amended rule filings under part 40 per § 150.10(a)(1), (a)(6). | 6 | 2 | 12 | 5 | 60 |
| Exchange .. | New or amended rule filings under part 40 per § 150.11(a)(1), (a)(5). | 6 | 2 | 12 | 5 | 60 |
| Exchange .. | Collection, review, and disposition of application per § 150.9(a). | 6 | 325 | 1,950 | 7 | 13,650 |
| Exchange .. | Collection, review, and disposition of application per § 150.10(a). | 6 | 85 | 510 | 7 | 3,570 |
| Exchange .. | Collection, review, and disposition of application per § 150.11(a). | 6 | 90 | 540 | 7 | 3,780 |
| Exchange .. | Summaries Posted Online per § 150.9(a) .... | 6 | 30 | 180 | 7 | 1,260 |
| Exchange .. | Summaries Posted Online per § 150.10(a) .. | 6 | 10 | 60 | 7 | 420 |
| Exchange .. | § 150.9(b) Recordkeeping ........................... | 6 | 1 | 6 | 30 | 180 |
| Exchange .. | § 150.10(b) Recordkeeping ......................... | 6 | 1 | 6 | 30 | 180 |
| Exchange .. | § 150.11(b) Recordkeeping ......................... | 6 | 1 | 6 | 30 | 180 |
| Exchange .. | § 150.9(c)(1) Weekly Report ....................... | 6 | 52 | 312 | 6 | 1,872 |
| Exchange .. | § 150.10(c)(1) Weekly Report ..................... | 6 | 52 | 312 | 6 | 1,872 |
| Exchange .. | § 150.11(c) Weekly Report .......................... | 6 | 52 | 312 | 6 | 1,872 |
| Exchange .. | § 150.9(c)(2) Monthly Report ...................... | 6 | 12 | 72 | 6 | 432 |
| Exchange .. | § 150.10(c)(2) Monthly Report .................... | 6 | 12 | 72 | 6 | 432 |
| Exchange .. | § 150.2(a)(3)(ii) DS Estimate Submission Petition. | 6 | 4 | 24 | 1 | 24 |
| Exchange .. | § 150.2(a)(3)(ii) DS Estimate Submission .... | 6 | 4 | 24 | 20 | 480 |
| Exchange .. | § 150.5(a)(2)(ii) Exchange-Set Limit Exemption Application. | 6 | 425 | 2,550 | 2 | 5,100 |
| Market Participant. | § 150.5(a)(2)(ii) Exchange-Set Limit Exemption Application. | 425 | 1 | 425 | 2 | 850 |
| Market Participant. | § 150.9(a)(3) NEBFH Application ................. | 325 | 2 | 650 | 4 | 2,600 |

[1464] *See* CL–ICE–60929 at 17.

[1465] The Commission has combined the burdens for recordkeeping under §§ 150.9(c), 150.10(c), and 150.11(c). Table IV–B–1 at the end of this section provides a more detailed breakdown of costs by regulation.

[1466] The Commission has combined the burdens for recordkeeping under §§ 150.9(c)(2) and 150.10(c)(2). Table IV–B–1 at the end of this section provides a more detailed breakdown of costs by regulation.

TABLE IV–B–1—BREAKDOWN OF BURDEN ESTIMATES BY REGULATION AND TYPE OF RESPONDENT—Continued

| Type of respondent<br>A | Required record or report<br>B | Total number of respondents<br>C | Annual number of responses per respondent<br>D | Total annual responses<br>E [1467] | Estimated number of burden hours per response<br>F | Annual burden<br>G [1468] |
|---|---|---|---|---|---|---|
| Market Participant. | § 150.10(a)(3) Spread Exemption Application. | 85 | 2 | 170 | 3 | 510 |
| Market Participant. | § 150.11(a)(2) Application On Form 704 | 90 | 2 | 180 | 3 | 540 |
| Market Participant. | § 150.3(g) Recordkeeping | 425 | 50 | 21,250 | 1 | 21,250 |
| Market Participant. | § 19.01(a)(1) Form 504 | 40 | 12 | 480 | 15 | 7,200 |
| Market Participant. | § 19.01(a)(2)(i) Form 604 Non Spot Month | 250 | 10 | 2,500 | 30 | 75,000 |
| Market Participant. | § 19.01(a)(2)(ii) Form 604 Spot Month | 100 | 10 | 1,000 | 20 | 20,000 |
| Market Participant. | § 19.02 Form 304 | 200 | 52 | 10,400 | 1 | 10,400 |
| Market Participant. | § 19.01(a)(3) Form 204 | 425 | 12 | 5,100 | 3 | 15,300 |
| Market Participant. | § 150.3(h) Special Call | 425 | 1 | 425 | 2 | 850 |
| Market Participant. | § 150.7(a) Form 704 Initial Statement | 250 | 1 | 250 | 15 | 3,750 |
| Market Participant. | § 150.7(a) Form 704 Annual Update | 250 | 1 | 250 | 8 | 2,000 |
| Totals | | 431 | 116.13 | 50,052 | 3.91 | 195,734 |

[1467] Column C times column D.
[1468] Column E times column F.

4. Initial Set-Up and Ongoing Maintenance Costs

In documents submitted to OMB in accordance with the requirements of the Paperwork Reduction Act, the Commission estimated that the total annualized capital, operational, and maintenance costs associated with complying with the proposed rules amending part 150 would be approximately $11.6 million across approximately 400 firms. Of this $11.6 million, the Commission estimated that $5 million would be from annualized capital and start-up costs and $6.6 million would be from operating and maintenance costs. These cost estimates were based on Commission staff's estimated costs to develop the reports and recordkeeping required in the proposed part 150.

The Commission explained that the proposed expansion of the number of contract markets with Commission-set position limits, and the Congressional determination that such limits be applied on an aggregate basis across all trading venues and all economically-equivalent contracts, might increase operational costs for traders to monitor position size to remain in compliance with federal position limits. The Commission further explained that as such limits have been in place in the futures markets for over 70 years, the Commission believed that traders in those markets would have already developed means of compliance and thus would not require additional capital or start-up costs. The Commission stated its expectation that, while affected futures entities would be able to significantly leverage existing systems and faculties to comply with the extended regime, entities trading only or primarily in swaps contracts may not have developed such means.

One commenter provided specific estimates of the start-up costs to develop new systems to track and report positions, stating that per-entity costs will range from $750,000 to $1,500,000. The commenter also stated that ongoing annual costs would range from $100,000 to $550,000 per entity.[1469] The Commission notes that the commenter did not provide data underlying its cost estimates from which the Commission could duplicate the commenter's estimates.

The Commission maintains its belief that market participants will be able to leverage existing systems and strategies for tracking and reporting positions. As noted above, the Commission recognizes that expanding the federal speculative position limits regime into additional commodities beyond the legacy agricultural commodities will increase monitoring costs for firms. However, the Commission continues to expect that firms trading in the commodities subject to federal limits under § 150.2 do currently monitor for exchange-set and/or federal limits, and submit reports to claim exemptions in contracts for future delivery in such commodities. The Commission therefore continues to believe that costs for futures market participants resulting from the rules adopted herein are marginal increases upon existing costs, rather than entirely new burdens. Further, the Commission notes that it is difficult to ascertain an estimate of the average cost to market participants, as, depending on its size and complexity, a market participant could comply with position limits using anything from an Excel spreadsheet to multiple transaction capture systems.

The Commission is increasing its estimates to respond to the commenter. For swaps market participants unused to speculative position limits on swaps contracts, the Commission continues to estimate a greater cost to start and continue monitoring for and complying with speculative position limits.

Specifically, the Commission estimates that 441 entities would incur annualized start-up costs across all affected entities of $47,800,000. The

[1469] *See* CL–FIA–59595 at 35–36.

Commission also estimates that 441 entities would incur ongoing operating and maintenance costs of $12,075,000 across all affected entities. The Commission invites comments on its estimates. Table IV–B–2 breaks down the start-up and annual operating and maintenance costs by affected entities.

TABLE IV–B–2—BREAKDOWN OF START-UP AND ANNUAL OPERATING AND MAINTENANCE COSTS

| | Total number of respondents | Total annualized capital/start-up costs | Average annualized capital/start-up costs | Total annual operating & maintenance costs | Average annual (operating & maintenance costs) | Total annualized cost requested |
|---|---|---|---|---|---|---|
| §§ 19 and 150—Futures & Swaps Participants | 425 | 42,500,000 | 100,000 | 10,625,000 | 25,000 | 53,125,000 |
| §§ 19 and 150—Swaps Only Participants | 10 | 5,000,000 | 500,000 | 1,000,000 | 100,000 | 6,000,000 |
| § 150—Exchanges | 6 | 300,000 | 50,000 | 450,000 | 75,000 | 750,000 |
| Total | ........................ | 47,800,000 | ........................ | 12,075,000 | ........................ | 59,875,000 |

5. Request for Comment

The Commission invites the public and other Federal agencies to comment on any aspect of the reproposed information collection requirements discussed above. The Commission will consider public comments on this reproposed collection of information in:

(1) Evaluating whether the reproposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information will have a practical use;

(2) evaluating the accuracy of the estimated burden of the reproposed collection of information, including the degree to which the methodology and the assumptions that the Commission employed were valid;

(3) enhancing the quality, utility, and clarity of the information proposed to be collected; and

(4) minimizing the burden of the reproposed information collection requirements on registered entities, including through the use of appropriate automated, electronic, mechanical, or other technological information collection techniques, *e.g.,* permitting electronic submission of responses.

Copies of the submission from the Commission to OMB are available from the CFTC Clearance Officer, 1155 21st Street NW., Washington, DC 20581, (202) 418–5160 or from *http://RegInfo.gov.* Organizations and individuals desiring to submit comments on the reproposed information collection requirements should send those comments to:

• The Office of Information and Regulatory Affairs, Office of Management and Budget, Room 10235, New Executive Office Building, Washington, DC 20503, Attn: Desk Officer of the Commodity Futures Trading Commission;

• (202) 395–6566 (fax); or

• *OIRAsubmissions@omb.eop.gov* (email).

Please provide the Commission with a copy of submitted comments so that all comments can be summarized and addressed in the final rulemaking, and please refer to the **ADDRESSES** section of this rulemaking for instructions on submitting comments to the Commission. OMB is required to make a decision concerning the proposed information collection requirements between 30 and 60 days after publication of this Release in the **Federal Register**. Therefore, a comment to OMB is best assured of receiving full consideration if OMB receives it within 30 calendar days of publication of this Release. Nothing in the foregoing affects the deadline enumerated above for public comment to the Commission on the Reproposal.

### *C. Regulatory Flexibility Act*

The Regulatory Flexibility Act (''RFA'') requires that agencies consider whether the rules they propose will have a significant economic impact on a substantial number of small entities and, if so, provide a regulatory flexibility analysis respecting the impact.[1470] A regulatory flexibility analysis or certification typically is required for ''any rule for which the agency publishes a general notice of proposed rulemaking pursuant to'' the notice-and-comment provisions of the Administrative Procedure Act, 5 U.S.C. 553(b).[1471] The requirements related to the proposed amendments fall mainly on registered entities, exchanges, FCMs, swap dealers, clearing members, foreign brokers, and large traders. The Commission has previously determined that registered DCMs, FCMs, swap dealers, major swap participants, eligible contract participants, SEFs, clearing members, foreign brokers and large traders are not small entities for purposes of the RFA.[1472]

One commenter, the NFP Electric Entities,[1473] stated that the Commission ''ignore[d] its responsibilities under the RFA'' because it did not account for the impact on the members of the trade associations. The commenter states that the rules impose costs on ''small entities'' that ''should not be swept up in the Commission's new speculative position limits.'' [1474] The Commission notes, however, that under the Between NFP Electrics Exemptive Order certain delineated non-financial energy transactions between certain specifically defined entities were exempted, pursuant to CEA sections 4(c)(1) and 4(c)(6), from all requirements of the CEA and Commission regulations issued thereunder, subject to certain anti-fraud, anti-manipulation, and record inspection conditions.[1475] All entities

[1470] 44 U.S.C. 601 *et seq.*

[1471] 5 U.S.C. 601(2), 603–05.

[1472] *See* Policy Statement and Establishment of Definitions of ''Small Entities'' for Purposes of the Regulatory Flexibility Act, 47 FR 18618–19, Apr. 30, 1982 (DCMs, FCMs, and large traders) (''RFA Small Entities Definitions''); Opting Out of Segregation, 66 FR 20740–43, Apr. 25, 2001 (eligible contract participants); Position Limits for Futures and Swaps; Final Rule and Interim Final Rule, 76 FR 71626, 71680, Nov. 18, 2011 (clearing members); Core Principles and Other Requirements for Swap Execution Facilities, 78 FR 33476, 33548, Jun. 4, 2013 (SEFs); A New Regulatory Framework for Clearing Organizations, 66 FR 45604, 45609, Aug. 29, 2001 (DCOs); Registration of Swap Dealers and Major Swap Participants, 77 FR 2613, Jan. 19, 2012, (swap dealers and major swap participants); and Special Calls, 72 FR 50209, Aug. 31, 2007 (foreign brokers).

[1473] The NFP Electric Entities is a group of trade associations related to electricity entities comprised of the National Rural Electric Cooperative Association, the American Public Power Association, and the Large Public Power Council, with the support of ACES and The Energy Authority.

[1474] *See* CL–NFP–59690 at 26–27.

[1475] *See* the Between NFP Electrics Exemptive Order (Order Exempting, Pursuant to Authority of the Commodity Exchange Act, Certain Transactions Between Entities Described in the Federal Power Act, and Other Electric Cooperatives, 78 FR 19670 (Apr. 2, 2013) (''Federal Power Act 201(f) Order'').

Continued

that meet the requirements for the exemption provided by the Federal Power Act 201(f) Order are, therefore, already exempt from position limits compliance for all transactions that meet the Order's conditions.

Further, while the requirements under this rulemaking may impact non-financial end users, the Commission notes that position limits levels apply only to large traders. Accordingly, the Chairman, on behalf of the Commission, hereby certifies, on behalf of the Commission, pursuant to 5 U.S.C. 605(b), that the actions proposed to be taken herein would not have a significant economic impact on a substantial number of small entities. The Chairman made the same certification in the December 2013 Position Limits Proposal [1476] and the 2016 Supplemental Position Limits Proposal.[1477]

## V. Appendices

### *A. Appendix A—Review of Economic Studies* [1478]

Introduction

There are various statistical techniques for testing various hypotheses about position limits and related matter. Many of these techniques are deployed to determine whether speculative positions influence price, price changes, or volatility. The Commission has engaged in a comprehensive review and analysis of the various economic studies and papers in the administrative record.

These economic studies bearing on the proposed rule arrived in the administrative record in various ways. They include studies cited in the Commission's notice of proposed rulemaking; studies substantially relied upon in comment letters; and studies mentioned in a list submitted by commenter Markus Henn (''Henn Letter'').[1479] Those studies that were submitted formally for the record receive focused discussion in Section IV below.

As a group, these studies do not show a consensus in favor of or against position limits. Many studies limited themselves to subsidiary questions and did not direct address the desirability or utility of position limits themselves. The quality of the studies varies. Some studies are written by esteemed economists and published in academic, peer-reviewed journals. For other studies, that is not the case. Those studies that did at least touch on position limits had disparate conclusions on the ability economists to use market fundamentals to explain commodity prices; the existence of ''excessive speculation'' in various futures markets; and the utility of position limits. Section 4a(a)(1) of the CEA provides for position limits as a means to address certain specified burdens on interstate commerce. Studies that dispute the utility of position limits for the purposes Congress identified are less helpful than studies addressing other questions.

Preliminary Matters

1. Defining ''Speculation'' and Use of Proxies To Measure Speculation

It can be difficult to distinguish between ordinary speculation that is permitted and desirable, because it facilitates the transfer of risk and provides liquidity for hedgers, and harmful or ''excessive'' speculation. Ideally, speculation may better align prices with market fundamentals.[1480] Speculators in the commodity futures market can generally enhance liquidity and reduce a hedger's cost associated with searching for a counterparty who wants to take an opposition position. Speculators facilitate the needs of hedgers to transfer price risk and increase overall trading volume, all of which can generally contribute to the well-being of a marketplace.[1481]

Congress has found ''excessive speculation'' in futures contracts to be ''an undue and unnecessary burden on interstate commerce.'' [1482] In accordance with that finding, Congress has provided for position limits in order to ''diminish, eliminate, or prevent such burden.'' This paper evaluates economic studies concerning how position limits can diminish unreasonable price fluctuations and changes.

a.''Excess Speculation'' and Volatility

Although volatility may be an indicator of excess speculation, as Congress has determined, price volatility, in itself, does not establish ''excess speculation.'' [1483] Changes in fundamentals of supply and demand can create substantial volatility, and some commodities are, based on their nature, more prone to price volatility. Changes in these fundamentals may induce disagreement between market participants on the appropriate price, causing some measure of price volatility, but this does not necessarily imply the existence of excess speculation.

One of the main functions of the swaps and futures markets is to permit parties with structural exposure to price risk (hedgers such as buyers or sellers of commodity-related products) to manage price changes or price volatility by transferring price risk to others. Speculators in these markets often, in effect, shield hedgers from some forms of price volatility by accepting this price risk. The nation's futures and swaps markets helps producers and suppliers of these commodities, and the customers they serve, hedge price risk to avoid price uncertainty when desired. In this way, volatility and speculation are not *per se* unwelcome phenomena in these markets. They are natural events in these markets. It is the nature of markets to fluctuate.[1484]

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*See also* CL–NFP–59690 at 14–15. The Federal Power Act 201(f) Order exempted all ''Exempt Non-Financial Energy Transactions'' (as defined in the Federal Power Act 201(f) Order) that are entered into solely between ''Exempt Entities'' (also as defined in the Federal Power Act 201(f) Order, namely ''any electric facility or utility that is wholly owned by a government entity as described in the Federal Power Act ('FPA') section 201(f) . . .; (ii) any electric facility or utility that is wholly owned by an Indian tribe recognized by the U.S. government pursuant to section 104 of the Act of November 2, 1994 . . .; (iii) any electric facility or utility that is wholly owned by a cooperative, regardless of such cooperative's status pursuant to FPA section 201(f), so long as the cooperative is treated as such under Internal Revenue Code section 501(c)(12) or 1381(a)(2)(C), . . . and exists for the primary purpose of providing electric energy service to its member/owner customers at cost; or (iv) any other entity that is wholly owned, directly or indirectly, by any one or more of the foregoing.''). *See* Federal Power Act 201(f) Order at 19688.

[1476] *See* December 2013 Position Limits Proposal, 78 FR at 75784.

[1477] *See* 2016 Supplemental Position Limits Proposal, 81 FR at 38499.

[1478] Earlier this year, a draft literature review written by staff was released prematurely. Although there are similarities between the analysis in that document and the analysis herein, that document did not represent the final views of the Commission or the Office of the Chief Economist.

[1479] February 10, 2014, comment letter by Markus Henn of World Economic, Ecology & Development, including an attachment, a November 26, 2013 list entitled ''Evidence on the Negative Impact of Commodity Speculation by Academics, Analysis and Public Institutions.'' *See http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=59628&SearchText=henn.* As noted, of the various economic studies and papers in the administrative record, some were cited in the December 2013 Position Limits Proposal. Others were substantially relied upon in comment letters or mentioned in a list submitted by commenter Markus Henn (CL–WEED–59628); these studies are available in the comment letter file through the Commission's Web site at *http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1708.*

[1480] Speculation is a natural market phenomenon in a market with differing investor expectations. Harrison and Kreps, Speculative Investor Behavior in a Stock Market with Heterogeneous Expectations, Quarterly Journal of Economics (Oxford University Press 1978).

[1481] Bahattin Büyükşahin and Jeffrey H. Harris, The Role of Speculators in the Crude Oil Futures Market (working paper 2009).

[1482] 7 U.S.C. 6a(a)(1).

[1483] *Id.*

[1484] What may be ''natural'' volatility in one commodity futures market may be unexpected in

Just as volatility is not a per se harmful or unexpected event in the commodity futures markets, speculation in those markets is welcome and will often actually reduce volatility. A well-reasoned 2009 economic study (by economists who were then CFTC employees) concluded that speculative trading in the futures market is not, in and of itself, destabilizing.[1485] This frequently cited study concludes that normal speculative trading activity actually reduces volatility levels, as a general rule, while acknowledging that there are limited empirical studies on the subject. ''The limited nature of the previous literature on the market impact of speculators can be attributed to the difficulty of obtaining data on their trading activities.'' [1486] There is, however, substantial theoretical literature that predicts that profitable speculation has a stabilizing effect, ''since speculators buy when the price is low, therefore, increasing depressed prices, and sell when the price is high, therefore, decreasing inflated prices.'' [1487]

Some economic studies attempt to distinguish between normal and helpful speculative activity and excessive speculation: between normal volatility and, in the words of the Commodity Exchange Act, ''unreasonable fluctuations'' in price.[1488] Part of the research task before any economist studying markets for excessive speculation is to model and interpret excessive speculation and unwanted volatility so as to distinguish between unwanted phenomena and the proper workings of a well-functioning market.

b. Working's Speculative T Index

While there is no well-established economic definition of ''excess speculation,'' many economists studying commodity futures marketplace have used a proxy for speculation in commodity futures marketplace known in the economic literature as the Working's speculative T index. Economist Holbrook Working devised in 1960 a ratio to measure the adequacy or excessiveness of speculation. As applied to commodity futures positions, the speculative T index is used to assess the amount of speculative positions in the marketplace beyond the amount of speculative positions necessary to provide liquidity for hedgers in the marketplace.[1489]

The Working's speculative T index is calculated as follows:

$$T = \begin{cases} 1 + \frac{SS}{HL+HS} & if\ HS \geq HL \\ 1 + \frac{SL}{HL+HS} & if\ HL \geq HS \end{cases}$$

where SS is short speculator (non-commercial) positions, SL is long speculator positions, HS is short hedge (commercials) positions and HL is long hedge positions.

It is calculated by computing the ratio of long and short positions for all trades in the commodity market, including those of hedgers and those of speculators.[1490] A high ratio indicates many speculators are holding commodity futures positions. When this speculative T-index is included as an economic variable in economist's models to explain prices, economists may interpret the T index to be a proxy for the relative amount of speculation in the marketplace.

A high Working T index is one way to quantify excess speculation in technical terms, but even then that may not translate into excessive speculation in ''economic terms.''[1491] Additional economic analysis or historical comparisons are useful to understand the meaning and impact of a relatively high number of speculators in a market place.[1492]

c. Absence of Consensus on ''Price Bubbles''

There are several published studies on the effect of speculation on prices and price volatility, as well as studies on speculation generally. These studies employ various statistical methodologies. Some of these find the existence of ''price bubbles,'' meaning somehow artificially high prices that last longer than they should. These studies are analyzed below, but there is no academic consensus on what a ''price bubble'' is and how it can be detected. Thus many of the interpretations set forth in the ''price bubble'' studies are not the only plausible explanation for their statistical findings.

As further detailed below, there is no broad academic consensus on the economic definition of ''excess speculation'' or ''price bubble'' in commodity futures markets. There is also no broad academic consensus on the best statistical model to test for the existence of excess speculation. There is open skepticism in many economic quarters that there can even exist a significant ''price bubble'' in commodity futures markets.[1493]

A large measure of the difficulty stems from the difficulties of second-guessing the market's determination of the price of a commodity contract:

> Experts may express opinions about what the fundamental price should be, given current supply and demand conditions, but

another. Some critics of the proposed rule emphasize that different commodity markets behave differently, and that not all of the commodity markets referenced in the rule are likely to behave as the crude oil markets did in the 2006–2009 time period. On the other hand, some economic studies suggest there can be ''spillovers'' or transmission of volatility from one commodity market to the next. *See, e.g.,* Du, Yu, and Hayes, *Speculation and Volatility Spillover in the Crude Oil and Agricultural Commodity Markets: A Bayesian Analysis,* Energy Economics (2012).

[1485] Brunetti and Büyükşahin, *Is Speculation Destabilizing?* (working paper 2009). The Commission cited this study in particular in its December 2013 Position Limits Proposal. In addition, a copy of this economic study was formally submitted by the CME Group, Inc., as part of the administrative record in a March 28, 2011 comment.

[1486] *Id.* at 3.

[1487] *Id.* at 5.

[1488] 7 U.S.C. 6a(a)(1).

[1489] *See* Bahattin Büyükşahin and Jeffrey H. Harris, *The Role of Speculators in the Crude Oil Futures Market,* at 9 n.7, 10–11 & 24 (working paper 2009) (employing this technique).

[1490] The Working speculative index is ''predicated on the fact that long and short hedgers do not always trade simultaneously or in the same quantity, so that speculators fill the role of satisfying unmet hedging demand in the marketplace. *Id.* at 1.

[1491] *Id.* at 10.

[1492] *See id.* at 9–10 (a speculative index of 1.41 for crude oil futures contracts in 2008 meant that share of speculation beyond what was minimally necessary to meeting short and long hedging needs, was 41 percent: while such a percentage may seem on its face ''potentially alarming,'' it is comparable historically with agricultural commodity markets).

[1493] Dwight R. Sanders & Scott H. Irwin, *A speculative bubble in commodity futures prices? Cross-sectional evidence,* 41 Agricultural Economics 25–32 (2010) (arguing that while ''bubble'' explanations ''are deceptively appealing, they do not generally withstand close examination''). Because commodity index fund buying is very predictable, it seems highly unlikely that in ordinary market environment traders would fail to trade against an index fund if the fund were driving prices away from fundamental values.

a basic axiom of classical economics is that free markets do a better job of weighing information and determining prices that any group of experts.[1494]

Nonetheless, there are statistical techniques, and theoretical models, that economists have employed to attempt to discern whether recent behavior in the nation's commodity futures markets has deviated from what can be reasonably ascribed to the fundamentals of supply and demand.

d. The Project: Studying Whether Speculative Positions Causing Unwarranted Price Moves

In order to test for the presence of ''excessive'' speculation, many of these economic studies look to whether the existence of substantial positions by speculative traders causes price volatility or a semi-permanent change in price. The idea underlying these studies is that if the presence of sufficiently large positions can induce such price behavior, it is ''excessive.'' Economists use various statistical tools, including correlation analysis, to determine whether there is price behavior caused by speculative positions that is ''unwarranted.'' ''Unwarranted'' price movements are those not associated with fundamentals of supply and demand, the inherent volatility of market prices, or other factors independent of position.

In these studies, economists discuss whether positions have caused movements in price. Technically, economists will study ''price returns'' for a class of commodity, rather than just ''price'' (the nominal price level). Price return gives one the change in price over time, divided by price.[1495]

$$\text{A price return is } \frac{P_{t+1}-P_t}{P_t}.$$

Price return measures price changes over the scale of the underlying price. That is, different commodities may have entirely different scales for prices; by dividing by the underlying price, price returns put different commodity classes on the same percentage scale for comparison purposes.

The conclusions of these various economic analyses, discussed in detail in Section III below, have achieved a reasonable measure of academic consensus on some subsidiary matters bearing on the ultimate question of whether excessive speculation has had an impact on the commodity futures markets. However, there is no academic consensus on the ultimate question of the extent and breadth of the impact, and there is no singular economic study of compelling persuasiveness.

2. Dearth of Compelling Empirical Studies on the Effect of Position Limits on Prices or Price Volatility

There are not many compelling, peer-reviewed economic studies engaging in quantitative, empirical analysis of the impact of position limits on prices or price volatility, and thus on whether position limits are useful in curbing excessive speculation.[1496] The limitations that inhere in empirical analysis of this complex question are set forth below.

a. Trader Identity and Role: Incomplete Data

As many economic researchers observe in their studies, there is no decisive accounting on whether a particular trade or set of trades is speculative or hedging. In practice, researchers often use a rough proxy based on the nature of the trader: Whether they are commercial or non-commercial. However, in both practice and theory, this proxy may fail: Commercial traders may speculate and non-commercial traders may well hedge. For example, a commercial trader might speculate and take an outsize position, in the sense that it exceeds a given hedging business need, in a commodity on the belief that the price will go up and down. Thus ''traders sometimes may be misclassified between commercial and noncommercial positions, and some traders classified as commercial may have speculative motives.'' [1497]

Further compounding these classification problems, the publicly available data also aggregates traders' positions across maturity dates for futures contracts, while the price for any given commodity futures contract is not aggregated by maturity.[1498] In addition, section 8 of the Commodity Exchange Act limits the distribution of detailed trade positon data to academic researchers. The identity of individual traders for specific trades, and their position in the market at the time of name, is not disseminated publicly to economic researchers.[1499] Thus, even when a position limit breach occurs, it is difficult to measure the impact on individual participants in the marketplace.

Even when an economic researcher can find detailed information on specific trades and the nature of the traders, that might not be sufficient to characterize an individual trade as hedging or speculative. A market participant may have business needs it hedges with derivatives and also engage in speculative trading. Thus the identity of the market participant purchasing the commodity futures contracts alone does not accurately capture the motivation for or purpose of the trade. Thus, an economic researcher faces significant data constraints in reliably characterizing trades as speculative or hedging, making it difficult to determine whether position limits are useful in curbing certain speculative activity.

b. Limitations on Studying Markets With Pre-Existing Position Limits

Designing an economic study of the effect of position limits is complicated by the fact that for many commodity markets, position limits are already in place. There is therefore not reliable empirical data for how certain modern commodity futures markets would operate in the absence of position limits. For all the agricultural commodities referenced in the rule, the futures markets have already had in place spot-month position limits at least as strict as those proposed in the rule. For energy commodities such as crude oil, there have been pre-existing ''accountability levels,'' meaning an exchange has the option (but not the requirement) to ask a trader to reduce its position if it exceeds a certain level. For crude oil, the current all-months-combined accountability level is 20,000 contracts. The position limit in the proposed rule for the all-months-combined limit is 109,200 contracts.

The existence of binding position limits in agricultural commodities and accountability levels in the energy markets does not mean that traders do not transgress these limits in current markets and take outsized market positions for speculative reasons. But the existence of current limits does make the economist's task of measuring position limit impact more difficult. When an economist studies an agricultural futures market and attempts to assess the economic advantages and disadvantages of imposing position limits, he or she does not have a dataset of market prices in a marketplace

[1494] D. Andrew Austin & Mark Jickling, *Hedge Fund Speculation and Oil Prices* (1 ed. 2011).

[1495] P is price and t is a particular time, with t+1 being the point in time that is one fixed increment away over which the return is being computed.

[1496] As noted above, however, CEA section 4a(a) reflects the underlying assumption that position limits may be useful for that purpose.

[1497] International Monetary Fund, *IMF Global Financial Stability Report: Financial Stress and Deleveraging: Macrofinancial Implications and Policy* (Oct. 2008).

[1498] *Id.*

[1499] Julien Chevallier, *Price relationships in crude oil futures: new evidence from CFTC disaggregated data,* 15 Environmental Economics and Policy Studies 135 (2012).

without position limits. Thus economists are dependent upon economic models and model interpretation when they attempt to describe how a marketplace without position limits would function. Many economic studies do not account in their models for pre-existing position limits or accountability levels. In fact, many economic studies that bear on the rulemaking do not endeavor to reach the ultimate question of the impact of position limits on prices and market dynamics at all.

There may be fewer instances of dramatic, large-scale ''excessive speculation'' because position limits have been in place in many of these commodity futures markets since 1938. There have thus been few opportunities to study the effect of the imposition of a position limits rule.[1500]

c. Inherent Difficulties of Modelling Complex Economic Phenomena

There is no singularly persuasive study, because these studies use economic models that are, by nature, simplifications of a complex reality. Each of the various models and statistical methods used in these diverse studies has advantages and disadvantages, but they deploy imperfect market data to answer ambitious and complex economic questions. Given the data and modeling limitations, it is unreasonable to expect an economic model that is fulsome (extending to position limits and market speculation), accurate (accommodating and reflecting economic history), and predictive. This is particularly true in the context of market data involving volatile and complex events.

Some studies are better-designed and better-executed than others, which means that they used defensible models with transparent source data. These are discussed throughout this review. Much of the analysis below highlights the flexibility of model design choices and the sensitivity of the results to these modelling choices.

3. Staff-Level Congressional Determinations

There have been findings by policymakers that excessive speculation exists in various commodity futures markets, as the Commission observed in its notice of proposed rulemaking. For example, the Staff of the Permanent Subcommittee on Investigations of the Homeland Security and Government Affairs found [1501] that excessive speculation has had ''undue'' influence on wheat price movements,[1502] the natural gas market,[1503] and oil prices.[1504] Congress itself found ''excessive speculation'' in futures contracts to be ''an undue and unnecessary burden on interstate commerce.'' [1505]

These studies, like all the studies analyzed here, were undertaken in an absence of definitive economic definitions and tests for excessive speculation; limitations on data quality and availability; and the inherent difficulty of modelling complex phenomena.

*Discussion*

1. Empirical Studies: Economic Studies with Statistical Analysis Bearing on Speculative Positions in the Commodity Markets or Speculation Generally

Economic studies presented in the context of this rulemaking may involve theoretical models; statistical analysis based upon market data; and, most commonly, a combination of both. The economic studies using statistical methods can be categorized into basic statistical methods, such as models of fundamental supply and demand (and related methods), Granger causality, or other methods. The economic studies presented or cited in the comment letters in this rulemaking are best grouped and analyzed by the statistical method they employ, for there are advantages and disadvantages particular to each statistical method.

This discussion evaluates 244 papers in connection with the position limits rule: 133 studies submitted as comments or mentioned in the December 2013 Position Limits Proposal; over 100 additional studies or articles listed in the Henn Letter; and ten additional studies submitted by commenters not included in the above sets.

This group of 244 papers can be categorized below by statistical methodology: 36 Granger causality analyses; 25 comovement or cointegration analyses; 46 studies creating models of fundamental supply and demand; 8 switching regressions or similar analyses; 3 studies using eigenvalue stability analysis; 26 papers presenting theoretical models; and 73 papers that were primarily surveys of the economic literature, perhaps with some aspect of empirical testing or analysis.[1506]

a. Granger ''Causality''

i. Overview of the Granger Method

Below is a discussion of the 36 analyses employing the ''Granger'' or ''Granger causality'' method of statistical analysis. This discussion includes a description of the method and its advantages and disadvantages.

The Granger method seeks to find whether a linear correlation exists between two sets of data that are known as ''time series.'' An example of a time series would be a pair of numbers constituting future prices and time, with the time between the different future prices being a fixed amount of time. This fixed time is known as the ''time step.'' The Granger method takes two time series, such as Series A (futures price returns, each for a different time, for a fixed time step) and Series B

[1500] CFTC, *A Study of the Silver Market, Report To The Congress In Response To Section 21 Of The Commodity Exchange Act, Part Two,* 123 (May 19, 1981) (observing that the imposition of a position limit in silver futures contracts by the Chicago Board of Trade in 1979 did not raise prices); *id.* at 123–24 (observing that price reaction to position limits involves a variety of factors and ''it is not possible to predict in advance the effect of imposition of position limits'').

[1501] *See* Analysis, Section III(B), infra (discussing an economic analysis of these reports).

[1502] Permanent Subcomm. on Investigations of the U.S. Senate, Comm. on Homeland Sec. & Governmental Affairs, *Excessive Speculation in the Wheat Market,* (2009), *available at http://hsgac.senate.gov/public/_files/REPORTExcessiveSpecullationintheWheatMarketwoexhibitschartsJune2409.pdf.*

[1503] Permanent Subcomm. on Investigations of the U.S. Senate, Comm. on Homeland Sec. & Governmental Affairs, Excessive Speculation in the Natural Gas Market, (2007), *available at http://www.hsgac.senate.gov//imo/media/doc/REPORTExcessiveSpeculationintheNaturalGasMarket.pdf?attempt=2.*

[1504] Permanent Subcomm. on Investigations of the U.S. Senate, Comm. on Homeland Sec. & Governmental Affairs, *The Role of Market Speculation in Rising Oil and Gas Prices: A Need to Put the Cop Back on the Beat,* at 19–32 (2006) *available at http://www.hsgac.senate.gov//imo/media/doc/REPORTExcessiveSpeculationintheNaturalGasMarket.pdf?attempt=2* (finding increased speculation in energy commodities and an effect of speculation on prices).

[1505] 7 U.S.C. 6a(a)(1).

[1506] The remaining 27 papers fall into two groups. Two additional papers presented unique methodologies involving volatility are interwoven into the analysis below. The remaining twenty-five papers were not ultimately susceptible to meaningful economic analysis. These papers included pure opinion pieces, studies written in foreign languages, press releases, background documents on basic points of economics or law, studies unavailable due to broken hyperlinks that could not be resolved, or studies founded on methodologies too suspect to warrant extensive discussion. In the latter category, for example, was an unpublished study purported to use a ''novel source of information''—Google metrics involving user searches—as a proxy for the demand associated with ''corn price dynamics.'' Massimo Peri, Daniela Vandone & Lucia Baldi, *Internet, noise trading and commodity futures prices,* 33 International Review of Economics & Finance 82–89 (2014) (cited by Henn Letter). *See also,* Letter from Markus Henn, World Economic, Ecology & Development, to CFTC (Feb. 10, 2014). *See also,* Markus Henn, Evidence on the Negative Impact of Commodity Speculation by Academics, Analysis and Public Institutions, (Nov. 26, 2013).

(changes in speculative positions over the same time step). It then seeks to determine whether there is a linear correlation between Series A and Series B. This is done by using position data that is lagged over time.

For example, for the time of 12:00 p.m. and the price of $20 for a May cotton futures contract, the researcher using Granger ''causality'' would associate a position in May cotton futures from a set time prior to 12:00 p.m. If the time step were one minute, that time would be 11:59 a.m. The researcher performs a regression analysis on these two time series (price and time on the one side of the equation, and position and lagged time on the other). They estimate the correlation (technically, they look at the coefficient of the regression) through this analysis to come to a conclusion of whether, over that minute-interval, it can be said that there is a linear correlation between futures prices and positions.

While the Granger test is referred to as the ''Granger causality test,'' it is important to note that, notwithstanding this shorthand, ''Granger causality'' does not establish an actual cause-and-effect relationship. What the Granger method gives as a result is evidence of the existence of a linear correlation between the two time series or a lack thereof.

Moreover, the Granger method only tests for linear correlations. It cannot exclude causation associated with other statistical relationships.

The persuasiveness of a Granger study often turns on the soundness of the modelling choices, as discussed further in subsection 3 below.[1507]

ii. Advantages of the Granger Method

At the highest level, the Granger method is based on well-credentialed statistical methodology. It has been used for several decades by economists and its properties are well-established and well-debated in the economic literature. In that sense, unlike some of the other methods employed in this context, it has stood the test of time. It has been deployed in macroeconomics and financial economics.

The Granger test has several advantages. It is auditable in the sense that it can be fully replicated by a third party. The method is relatively simple to apply. It need not depend on complex mathematics. The method's straightforward approach permits a great deal of transparency in analyzing both inputs and results. Although the results can be highly sensitive to modelling choices, the modelling choices are made explicitly. That is, the equations that are used for the linear regression can easily be viewed together with the definitions for the variables.

iii. Disadvantages of the Granger Method

Not all statistical methods apply well to all situations. In the particular context of speculation and positions limits, application of the Granger methodology has some disadvantages and causes for concern. While the statistical answers are, by their nature, fairly precise, the drafting of the question and the economic interpretation of the results can cause problems. This limitation of the Granger method of course is shared with some other statistical methods. However, we discuss below why this is particularly true of Granger in the context of these studies on speculation and prices. Many of the potential problems in these studies do not so inhere so much in the method itself as in the modelling choices, other operational choices such as the length of time step and time lag, and the interpretation of the results.[1508] Below, we analyze why this is so.

First, the typical application of the Granger method in the studies review assumes a linear relation between the variables of interest: For example, prices and positions. The technique is useful for describing statistical patterns in data among variables ordered in time. But Granger does not claim to discuss simultaneous events. It is a statistical test which, in rough terms, says that if event A typically precedes event B, then event A ''Granger-causes'' event B. Granger is a statistical method for analyzing data for correlations, and ''Granger causation'' is not ''causation'' per se. It does not illustrate the method and means of actual causation nor does it claim to establish actual causation in reality.

For example, the Granger method cannot explain what causal mechanism links two events, events A and B, and a Granger model cannot detect all real-world causation. For example, an individual Granger model cannot conclude whether there is a relation between event A and event B that is ''hidden'' because the time step chosen is so long that the events look to occur simultaneously over the observed interval (be it a day or a week).

A second disadvantage concerns the sensitivity of the test to the time period studied. Especially in the context of the Granger method, the selection of the particular time internal is important to obtain the most useful results: Selection of too large a time period may hide correlations. Some of the position studies use daily price data, while others use weekly price data. When commodity prices are quite volatile, and positions are more gradual in changes, daily time steps may have greater unexplained variation in the commodity prices than when the time series for price data is constructed based on weekly sampling. A study by International Monetary Fund economists, using weekly data, observed that this time interval ''may hamper the identification of very short-run effects, given that the transmission from positions to prices may happen at higher frequency. Indeed, some market participants anecdotally suggest that there are short-run effects that may last only a matter of days.'' [1509]

Another potential problem is picking a time lag that is too short to detect possible market phenomenon. ''[K]nowing whether price changes lead or lag position changes over short horizons (a few days) is of limited value for assessing the price pressure effects of flows into commodity derivatives markets.'' [1510]

In the statistical calculations underlying the Granger method, this greater volatility may lead to a larger denominator in what is called the ''t-statistic,'' and that will in turn lead to a lower t-statistic (in absolute value). The t-statistic is used in the Granger method to assess how well a variable, such as positions, explains another variable, such as commodity prices. In this way, the selection of the time interval can easily affect the strength of the Granger method result.

A third disadvantage of Granger inheres in the selection of the time lag. A Granger analysis will not capture an effect that is delayed beyond the length of the time lag. And a Granger analysis with too long a time lag may not detect

[1507] *See generally* Grosche, *Limitations of Granger Causality Analysis To Assess the Price Effects From the Financialization of Agricultural Commodity Markets Under Bounded Rationality,* at 2–5 (Agricultural and Resource Economics 2012).

[1508] *See, e.g.,* Grosche, *Limitations of Granger Causality Analysis To Assess the Price Effects From the Financialization of Agricultural Commodity Markets Under Bounded Rationality* (Agricultural and Resource Economics 2012); Williams, *Dodging Dodd-Frank: Excessive Speculation, Commodities Markets, and the Burden of Proof,* Law & Policy Journal of the University of Denver (2015).

[1509] Antoshin, Canetti, and Miyajima, *IMF Global Financial Stability Report: Financial Stress and Deleveraging: Macrofinancial Implications and Policy,* Annex 1.2, Financial Investment in Commodities Markets at p. 65 (October 2008) (footnote and citation omitted).

[1510] Singleton, *The 2008 Boom/Bust in Oil Prices,* at 15 (working paper March 23, 2011) (''Of more relevance is whether flows affect returns and risk premiums over weeks and months.'') (footnote omitted).

price changes during periods of price volatility. The Granger technique does not guide the selection of the time lag. There are some heuristic techniques to help determine the time lag based on the ''goodness-of-fit'' [1511] of regressions, but these supplemental techniques may yield time lags that do not have a strong theoretical footing.[1512]

In such ways, and others, the authors of such study have wide license in modelling design. The results can be highly dependent upon and sensitive to model design choices. Key design decisions of seemingly little import, such as the selection of time steps, can in fact make a substantial difference in the study's result. While such flexibility can be useful, this flexibility also permits Granger results to be sensitive to modelling assumptions. Such sensitivity, especially in the particular context of the volatile commodity prices, is problematic. Volatility in commodity prices is a complex phenomenon, with possibly overlapping effects of short- and long-term volatility and many exogenous variables that can affect prices. In short, ''care must be taken not to overstate the interpretive power'' of Granger causality studies.[1513]

Finally, the method cannot discern the true cause of something when event A and B occur almost simultaneously. Granger cannot say whether A caused B or whether C causes A and then C causes B with a brief time lag. In this way, Granger correlation analysis is fundamentally incapable of establishing a cause and effect relationship.

There can also be limitations with regard to the data used in Granger studies on position limits, the majority of which used Commission data. There is a problem which inheres in this data in the particular context of position limit studies. The trade data used identifies the entity doing the trade as ''commercial'' or ''non-commercial.'' The data does not identify whether a particular trade is a hedge or a speculative gamble.[1514] While the studies' authors may infer that a trader's identity as a commercial trader is strongly associated with hedging (or at least non-speculative trades), in practice that may be far from the case.

There is also the statistical concept of ''robustness,'' meaning roughly that the results of a study are not qualitatively different based on different applications (different data sets, different tweaks of assumptions). In several ways, application of the Granger method in this particular context offers grounds for caution for study authors seeking statistical robustness. First, for a given time step and commodity, the particular time interval chosen may affect the result. Second, a Granger method is, by its nature, very sensitive to which particular dataset is chosen. Once again, a study's author(s) have wide discretion in the selection of which datasets to study, and Granger methodology will be highly sensitive to this selection.

There is the related problem of economic robustness. For example, because of individual market characteristics, a study limited to a particular commodity or time period may fail to detect patters that would be detectable applying the same method in to other time periods of commodities. Applying Granger analysis to commodity prices presents special challenges in this context because many commodity prices can be quite volatile, especially in the short-term. That is, the Granger method may have low ''statistical power'' in this context. In mathematical terms, high volatility in one of the Granger variables can lead to large standard errors for regression coefficients for the t-statistic.[1515]

A modelling choice to include other variables can further reduce the statistical power of the statistical test used in the Granger method.[1516] Other economic variables in the regression analysis, if not properly chosen, can compromise the Granger ''causality'' test. For instance, explanatory variables may not be uncorrelated to the speculative position or position change variables. To the extent that the variables are correlated to speculative positions, they may, in the estimation of the regression, wash out the price effect. The t-statistic of the regression coefficient remains small because the standard error estimate of the coefficient is large due to common correlation between explanatory variables.[1517]

Authors of Granger method studies may add ''control variables'' in order to reflect other factors that may be affecting or relevant to the two main variables of primary interest (such as price and position). The introduction of control variables will help to discount spurious corrections between the variables of primary interest by studying whether another variable could be correlated to (and thus ''Granger causing'') variables such as price and position. Adding extra variables can, on the one hand, affect for third factors which may be relevant. On the other hand, the introduction of the third factors may compromise the statistical power of the primary question of interest.

Finally, there are also economic studies casting doubt on the suitability of commodities data for meaningful Granger tests, given volatility in commodities price data.[1518] This is because volatility increases the standard error of the estimated coefficient for the lagged variable(s). Thus, Granger tests examining commodities data may lack statistical power to detect Granger causality.

iv. Comparison of Strengths and Weaknesses

Granger techniques provide great flexibility. This flexibility also provides great license to economists on selection of critical factors such as the length of the time lag and the time step. The ultimate conclusions of such studies may be influenced by model design. Unsurprisingly, different economists reach different results. In this sense, the conclusions of Granger-based papers are vulnerable to criticism.

v. Analysis of Studies Reviewed That Use Granger Methodology

Overall, when the Granger studies find a correlation (in the sense of a lead-lag relationship) between speculative positions and price returns, they do so not with respect to price returns as a whole, but the risk premium component of price returns. The risk premium is the portion of expected return of a futures contract associated with holding the contract. It is not an express term of the contract, but an amount that can be derived from economic analysis as the difference between the futures price return and a hypothesized price return

[1511] Roughly speaking, ''goodness-of-fit'' analyses examine how well the data fits the model. Using a goodness of fit criteria allows the data to select the number of lags that empirically fits the data the best.

[1512] *See generally* Williams, *Dodging Dodd-Frank: Excessive Speculation, Commodities Markets, and the Burden of Proof,* Law & Policy Journal of the University of Denver (2015) at 136–38 (discussing problems associated with Granger test's assumptions and parameters).

[1513] *Id.* at 138.

[1514] There are other difficulties in the CFTC dataset that complicate empirical analysis of herding activity. *See* Acharya, Ramadorai, and Lochstoer, *Limits to Arbitrage and Hedging: Evidence from the Commodity Markets,* at 19 (Journal of Financial Economics 2013).

[1515] *See* Bahattin Büyükşahin and Jeffrey H. Harris, *The Role of Speculators in the Crude Oil Futures Market* (working paper 2009) (later published in The Energy Journal, Vol. 32, No. 2, 167–202 (2011) under the title *Do Speculators Drive Crude Oil Futures Prices?*).

[1516] These test statistics is a t-test for one lag in the relevant variable or an F-test for multiple lags.

[1517] This argument is also correct for F-tests (a multivariable extension of t-tests).

[1518] David Frenk, Review of Irwin and Sanders 2010 OECD Report, at p. 6 (Better Markets June 20, 2010) and citations therein, cited in Henn Letter at 6–7.

for a futures contract. The risk premium is the return required to bear the undiversifiable risk on the relevant side of a futures contract.[1519]

There are also Granger studies that analyze speculative positions with respect to price returns as a whole or price volatility; these do not find a statistically significant correlation. Moreover, those studies that do find a lead-lag correlation using the Granger methodology in the risk premium context are limited to studies in particular markets in particular time frames: Studies using weekly, not daily, price data and analyzing crude oil and ethanol-related commodities (including wheat, which is an economic substitute for corn) during the 2007–2010 timeframe.

There are 36 primarily Granger-based economic studies in the administrative record. For analysis purposes, these papers are grouped according to whether they discuss primarily crude oil or other energy derivatives (8 studies); the possible impact of commodity index funds across multiple commodities (13); and agricultural commodities (15).

Crude Oil and Other Energy Derivatives

There was a substantial increase in crude oil prices through July 2008, followed by a significant price collapse from July 2008 through March of 2009.[1520] Several Granger analyses have looked at price returns and/or price volatility in the crude oil markets, or the energy markets generally, in the 2007–2009 timeframe.[1521]

Professor Kenneth Singleton found evidence that speculative positions Granger-caused risk premium on weekly time intervals during the 2007 to 2009 period when studying the crude oil futures markets.[1522] Part of Singleton's results were replicated in part in a paper by Hamilton and Wu using a different methodology than Granger causality analysis.[1523] Professor Singleton found a link between the volume of speculative positions and an increase in risk premium. Because risk premium is a component of price returns and hence price, he thus found a link—Granger causal link—between speculative positions and price. However, because risk premium is just a relatively small component of price, this study does not purport to explain entirely the large 2008 changes in crude oil prices.

In the case of index funds, many funds take long positions. The presence of large index funds positions raises an issue of whether what economists would call this ''heterogeneity of views'' can affect marketplace health. Singleton presents, with his Granger-like analysis, a discussion of heterogeneity in this context. He conjectures—without supporting empirical analysis—that learning about economic fundamentals with heterogeneous views may induce excessive price volatility, drift in commodity prices, and a tendency towards booms and busts. He asserts that under these conditions the flow of financial index investments into commodity markets may harm price discovery and thus social welfare.[1524]

Another paper using Granger analysis concluded that speculators did have an impact on price volatility in the crude oil market.[1525]

Some commenters have suggested that using a weekly, not a daily, time interval for a Granger analysis in this context is a better choice because speculative positions change gradually and there is, on a daily basis, substantial price volatility, especially in the crude oil market.[1526] The common sense explanation for this may be that prices change more often and more rapidly than position sizes, as a general rule. A weekly time interval is a good way to filter out price changes that speculative position changes cannot explain.[1527]

Other Granger analyses of the crude oil market use shorter time intervals and do not find Granger-causality between speculative position changes and either price returns, price changes or price volatility.[1528] The academic literature contains a divergence of views on whether the existence of ''excess speculation'' in the crude oil market would necessarily result in something that is easy to measure, like increases in oil inventories. Some economists argue against the role of ''excess speculation'' in crude oil, observing that when there was a run-up in prices of certain commodities, there was no noticeable increase in inventories.[1529] This assumes that a fundamental shock in the oil prices, for example, is likely to increase or decrease inventories, as hedgers in the physical market anticipate future price increases or decreases. However, other economists have explained that, at least in theory, speculation can affect spot oil prices without causing substantial increases in inventory (providing the price elasticity of oil demand is small).[1530]

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[1519] In theory, if the futures contract at expiration is a perfect substitute for the spot commodity, then the expiring futures price should converge to the spot price. It is important to note that many expiring futures contracts are imperfect substitutes for the spot commodity and this might prevent convergence. Moreover, the risk premium decreases to zero as the futures contract approaches expiration. Thus, the risk premium has no effect on the final convergence of the futures to the spot price at expiration of the futures contract, but could, in theory, impact the rate of convergence (although any impact may be negligible).

[1520] Bahattin Büyükşahin and Jeffrey H. Harris, *The Role of Speculators in the Crude Oil Futures Market* at 2 (working paper 2009).

[1521] *See, e.g.,* Goyal and Tripathi, *Regulation and Price Discovery: Oil Spot and Futures Markets* (working paper 2012); Irwin and Sanders, *Energy Futures Prices and Commodity Index Investment: New Evidence from Firm-Level Position Data* (working paper 2014); Kaufmann and Ullman, *Oil Prices, Speculation, and Fundamentals: Interpreting Causal Relations Among Spot and Futures Prices,* Energy Economics, Vol. 31, Issue 4 (July 2009); Kaufman, *The role of market fundamentals and speculation in recent price changes for crude oil,* Energy Policy, Vol. 39, Issue 1 (January 2011); Mobert, *Do Speculators Drive Crude Oil Prices?* (2009 working paper); Sanders, Boris, and Manfredo, *Hedgers, Funds, and Small Speculators in the Energy Futures Markets: An Analysis of the CFTC's Commitment of Traders Reports,* Energy Economics (2004); Singleton, *Investor Flows and the 2008 Boom/Bust in Oil Prices* (working paper March 23, 2011) (published in final form in Management Science in 2013); Singleton, *The 2008 Boom/Bust in Oil Prices* (working paper May 17, 2010).

[1522] Kenneth J. Singleton, *Investor Flows and the 2008 Boom/Bust in Oil Prices,* SSRN Electronic Journal 15 (2011) 18. (Equation 6, lagged correlation analysis that is, functionally, a Granger analysis).

[1523] Hamilton and Wu, *Risk Premia in Crude Oil Futures Prices,* Journal of International Money and Finance (2013) (replicating Singleton's result using a different methodology, a two-factor linear model of fundamental supply and demand).

[1524] Kenneth J. Singleton, *Investor Flows and the 2008 Boom/Bust in Oil Prices,* SSRN Electronic Journal 15 (2011) 5–8.

[1525] Jochen Möbert, Deutsche Bank Research, *Dispersion in beliefs among speculators* 9–10 (2009). This paper concluded that as net long positions increased, volatility increased. This paper was inconclusive of the impact of speculation on price levels (*id.* at 8–9), and observed caveats on the difficulty of accurate modelling in the complex crude oil market (*id.* at 11).

[1526] Frenk, *Review of Irwin and Sanders 2010 OECD Report,* at 6 (Better Markets June 10, 2010).

[1527] There are not many other economic studies in the administrative record duplicating the results of Singleton and Hamilton and Wu. A few others reached similar conclusions regarding the crude oil market using Granger analysis, but these are relatively modest or narrowly constructed studies that are not often cited by economic peers. *See* Goyal and Tripathi, *Regulation and Price Discovery: Oil Spot and Futures Markets* (working paper 2012) (concluding that regulations of the nation of India, including position limits, may have mitigated short duration ''bubbles'').

[1528] Kaufmann and Ullman, *Oil Prices, Speculation, and Fundamentals: Interpreting Causal Relations Among Spot and Futures Prices,* Energy Economics, Vol. 31, Issue 4 (July 2009); Kaufman, *The role of market fundamentals and speculation in recent price changes for crude oil,* Energy Policy, Vol . 39, Issue 1 (January 2011); Sanders, Boris, and Manfredo, *Hedgers, Funds, and Small Speculators in the Energy Futures Markets: An Analysis of the CFTC's Commitment of Traders Reports,* Energy Economics (2004).

[1529] Irwin and Sanders, *Index Funds, Financialization, and Commodity Futures Markets,* at 14–15, Applied Economic Perspectives and Policy (2010).

[1530] Hamilton, *Causes and Consequences of the Oil Shock of 2007–2008,* Brookings Paper on Economic Activity (2009); Parsons, *Black Gold & Fool's Gold: Speculation in the Oil Futures Market* at 82, 106–107 (Economia 2009) (if oil prices were

Irwin and Sanders conclude that there is no Granger-causation between positions in a particular commodity index fund and price returns in four energy commodity markets.[1531] Irwin and Sanders' paper contains a fairly robust Granger analysis which analyzes several models in conjunction with their standard model equation for position and price. However, all of the equations that they test for Granger causation contain a possible prejudice: The use of variables that may be correlated with price other than the position variable, thus masking the power of the position variable. Moreover, their paper fails to show that the particular index fund data they used was generally representative of index funds by statistical testing.[1532]

There is an earlier paper by Sanders, Boris, and Manfredo that has a similar result.[1533] However, this 2004 paper uses variables that may be correlated with price other than position data, and so, in the Granger analysis, the price equation used for Granger testing may mask some or all of the impact of positions on price (if any).[1534] As discussed, Irwin and Sanders' 2014 paper is also not completely free from this masking problem. However, it has only one, not several, variables that could mask correlation between position changes and price returns: A lagged price return variable. Irwin and Sanders, aware of the possibility of this masking of correlation, present a defense of their choice to include a lagged price return variable in their model. They argue that one does not know whether positions will affect just current price returns or both current and lagged price returns, and in this way it is not necessarily the case that there is a masking effect.

This argument does not prove that there is no masking effect. There is at least the concern that the Irwin and Sanders model, as constructed, masks possible Granger-causality between position changes and price returns. Theoretically, one could learn more by examining the linear correlation between explanatory variables (lagged price returns and changes in position) by performing additional diagnostic regressions. These regressions would estimate correlations between explanatory variables and resolve the open question of whether the price equation is significantly ''masking'' Granger-causality between position changes and price returns.

Selecting between competing models with divergent results becomes more of a judgment call than a science. Irwin and Sanders' 2014 paper is well-done, as are papers with opposite conclusions, which find an empirical relationship between position changes and price returns (risk premia), such as the Singleton Granger analysis discussed above, and a paper by Hamilton and Wu based on a different statistical method discussed below.[1535]

It is impossible to easily discern who is correct or what accounts for the difference in result. It could be the ''masking'' issue in the Irwin and Sanders model. It could also be the focus in the Irwin and Sanders work on price returns, as opposed to the focus in both Singleton's as well as Hamilton and Wu's on just a component of price returns, risk premia. Irwin and Sanders, by focusing on price returns, are doing Granger-causality testing with a model less sensitive to changes in just risk premia. The differing results could also be due to the different time horizons (weekly versus daily time increments) used in the competing studies.

This clash of well-executed studies is on an important issue—the dramatic changes in crude oil prices in 2006–2009. The study by Kaufman is not directly on point.[1536] He finds Granger-causation between different types of crude oil contracts, but does not look to positions or whether positions Granger-cause changes in price returns.

Kaufmann also finds that far-out futures contracts and spot crude oil are not correlated and he concludes that the reason for this lack of correlation is speculation in the crude oil market. However, there are gaps in this inference. Kaufmann assumes there should be a long-run equilibrium between the spot and the futures price but cannot discern a supply and demand reason for the lack of correlation. There are many factors of supply and demand that would lead to differences between far-out futures prices and spot prices in the crude oil market during the time period studied—1986–2007. These factors include the depletion of oil fields; variability in economic growth; discovery of new oil sources and better modes of extraction; adaption of oil infrastructure.[1537]

Index Funds Generally

Some economists have used the Granger methodology to study a group of commodity markets and to analyze, overall, the effect, or lack thereof, of commodity index fund investments on both energy and agricultural commodity prices.[1538] These relatively few Granger studies on the ''financialization'' effect vary in their conclusions. Overall, as a group, the Granger studies on the effect of index funds across a swath of

driven above the level determined by fundamental factors of supply and demand by forces such as speculation, storage would not necessarily increase, for ''successful innovations in the financial industry made it possible for paper oil to be a financial asset in a very complete way''); *accord* Lombardi and Van Robays, *Do Financial Investors Destabilize the Oil Price?*, at 21–22, European Central Bank Working Paper Series No. 1346 (June 2011). The ability drawdown or stock pile inventory is limited by storage capacity. Further, since it is expensive to store oil above ground, buy and hold strategies are only a loose constraint on prices.

[1531] Dwight R. Sanders & Scott H. Irwin, *Energy Futures Prices and Commodity Index Investment: New Evidence from Firm-Level Position Data,* 46 Energy Economics (working paper 2014).

[1532] In this paper, Irwin and Sanders critiqued Singleton's results, concluding that Singleton found Granger causation because he improperly calculated positon data. This debate cannot be resolved definitively. In the absence of better daily data on position in both swaps and position markets, it is unclear who is correct here.

[1533] Dwight R. Sanders, Keith Boris & Mark Manfredo, *Hedgers, funds, and small speculators in the energy futures markets: An analysis of the CFTC's Commitments of Traders reports,* 26 Energy Economics 425–445 (2004).

[1534] *Id.* at 439, Equation 5.

[1535] James D. Hamilton & Jing Cynthia Wu, *Risk premia in crude oil futures prices,* 42 Journal of International Money and Finance 9–37 (2014).

[1536] Robert K. Kaufmann, *The role of market fundamentals and speculation in recent price changes for crude oil,* 39 Energy Policy 105–115 (2011).

[1537] *Cf.* Kaufmann and Ullman, *Oil Prices, Speculation, and Fundamentals: Interpreting Causal Relations Among Spot and Futures Prices,* 31 Energy Economics (July 2009) (concluding that there is Granger-price causation between different types of crude oil). This study does not look for causation between position and price and so, again, is of marginal relevance in the position limits context.

[1538] *See, e.g.,* Antoshin, Canetti, and Miyajima, *IMF Global Financial Stability Report: Financial Stress and Deleveraging: Macrofinancial Implications and Policy,* Annex 1.2, Financial Investment in Commodities Markets (October 2008); Jeffrey H. Harris and Bahattin Büyükşahin, *The Role of Speculators in the Crude Oil Futures Market* (working paper 2009); Brunetti and Büyükşahin, *Is Speculation Destabilizing?* (working paper 2009); Frenk, *Review of Irwin and Sanders 2010 OECD Report* (Better Markets June 10, 2010); Gilbert, *Speculative Influences on Commodity Futures Prices, 2006–2008,* UN Conference on Trade and Development (2010) (page citations are to the 2009 working paper version placed in the administrative record); Gilbert, *Commodity Speculation and Commodity Investment* (powerpoint presentation 2010); Irwin and Sanders, *The Impact of Index and Swap Funds on Commodity Futures Markets: A Systems Approach,* Journal of Alternative Investments (2011); Irwin and Sanders, *The Impact of Index and Swap Funds on Commodity Futures Markets: Preliminary Results* (working paper 2010); Mayer, *The Growing Interdependence Between Financial and Commodity Markets,* UN Conference on Trade and Development (discussion paper 2009); Stoll and Whaley, Commodity Index Investing and Commodity Futures Prices (working paper 2010); Tse and Williams, *Does Index Speculation Impact Commodity Prices?,* Financial Review, Vol. 48, Issue 3 (2013); Tse, The Relationship Among Agricultural Futures, ETFs, and the US Stock Market, Review of Futures Markets (2012). A fairly late submission by Williams, *Dodging Dodd-Frank: Excessive Speculation, Commodities Markets, and the Burden of Proof,* Law & Policy Journal of the University of Denver (2015), studies generally the limitations of Granger causality.

commodity futures prices do not agree.[1539]

Gilbert concluded that commodity index fund positons did Granger-cause price increases in certain commodity futures markets during the 2006–2008 time period.[1540] Gilbert, a Professor of Economics at the University of Trento, Italy, found that this price impact appeared to be lasting or ''permanent.''[1541]

Gilbert's study is based upon a composed proxy for commodity fund index investments. The index data they use is not explained in sufficient detail in the paper and the results derived from this index are therefore not replicable.[1542] The price equation he uses for testing is problematic.[1543]

Gilbert's numerical results on price impact are dramatic, finding substantial average impact in various commodities due to speculation, with average impact in parts of 2008 of over 10 percent for aluminum, copper, nickel, wheat, and corn.[1544] Yet he provides little detail on how he arrived at these percentages other than to say that they are ''estimates'' that he inferred from the statistical results set forth in his Table 5.[1545] Because his findings are not well-documented and contain unexplained inferences, his paper is unreliable.

By contrast, the Granger analysis of Stoll and Whaley concludes that inflows and outflows from commodity index funds to the commodity markets do not have Granger-caused price changes in the commodity futures market.[1546] The authors of this study did find a fleeting price impact from when commodity index funds roll over to another contract month. (This fleeting rollover impact finding may be outdated; markets have learned to anticipate and account for index fund rollovers.)[1547]

Stoll and Whaley's analysis does not account for the possibility that there could be a delayed effect on futures price changes associated with a delay in laying off, in the futures markets, risks acquired in commodity index swap contracts. In practices, dealers may do this, acquiring risk in multiple markets within acceptable limits as they manage their portfolio risk.[1548] Moreover, a paper by Tse and Williams criticizes Stoll and Whaley's approach for using ''low frequency data'' and failing to use ''sufficiently granular data to capture fast futures markets dynamics.''[1549] Using intraday, shorter time intervals to analyze the possible effect of commodity fund investments in the futures markets, Tse and Williams conclude that there was ''transmission'' of price impacts from futures contracts in a particular commodity fund index (the GSCI index) to commodities that were not in the index. However, this Granger-causation result does not necessarily establish any price impact associated with excessive speculation. Other factors may lead to this result, such as time delay in illiquid markets, the role of the GSCI index as a price influencing mechanism, or the more rapid market response that tends to occur with more liquid markets.[1550]

While both the Stoll and Whaley and the Gilbert papers are often cited in the literature, they both have limitations in scope and approach. Other studies do not fully resolve this academic debate. In a paper by James W. Williams, the limitations of Granger causality analysis in the position limits context is discussed.[1551]

The general findings of Irwin and Sanders support Stoll and Whaley's conclusions.[1552] Irwin and Sanders analyzed weekly CFTC price data over a number of years and found that there was neither Granger-causation between index fund positions and futures price returns or Granger-causation between changes in fund positions and futures price volatility. Utilizing a Working's T-index, Irwin and Sanders also find that there was not excessive speculation in these markets.

Frenk criticizes Irwin and Sanders for (1) both their specific methodology, arguing that they used incorrect proxies for hedging volumes and (2) rehearsing the general disadvantages of using Granger analysis.[1553] Frenk identifies difficulties in Irwin and Sanders' data and underlying assumption.

There is a significant problem with the Irwin and Sanders paper. The price formula used for Granger testing in their paper is complex, incorporating many lagged price returns and lagged positions, and risks masking correlation due to the possible interdependence of

[1539] There are many more studies using the comovement or cointegration analysis, discussed in Section I(B) below, that look at the financialization questions.

[1540] Christopher L. Gilbert, *Speculative Influences on Commodity Futures Prices,* 2006–2008 (2010).

[1541] *Id.* at 23; *see also id.* at 24, Table 6 (average price impact by commodity, including a maximum price impact of over 16 percent for crude oil during 2006–2008 time period).

[1542] Several statements about the index in the paper indicate a lack of economic rigor, or at least major inferential leaps, in the assumption that the index approximates commodity index funds. *Id.* at 18, 21.

[1543] *See id.* at 22 (Equation 4) (complex equation that subtracts logarithmic prices without detailed economic justification for the destructive of data though subtraction).

[1544] *Id.* at 24, Table 6.

[1545] *See id.* at 23–24 (little or no statistical assessment of how the results of Table 4 and 5 results translate into the large price impact percentages in Table 6).

[1546] Hans R. Stoll & Robert E. Whaley, *Commodity Index Investing and Commodity Futures Prices* (working paper 2010).

[1547] Stoll and Whaley also found a divergence of futures and cash prices in wheat in 2006–2009 period, especially in 2008 period, but concluded that there were limited negative impacts on market functioning associated with this failure to diverge. This result should not be used to suggest that divergence is not a costly phenomenon. Stoll and Whaley's analysis is limited to CME's wheat futures contract. It failed to converge for a period of time because storage was mispriced in the contract during this time period, and market participants knew this and prices reflected this difference. CME eventually changed the wheat contract to charge a more appropriate amount for storage and the divergence phenomenon dissipated. So this example of divergence is associated with economic differences between the spot and futures contracts. It not an example of divergence associated with market manipulation, with attendant social welfare costs. *See* Frank Easterbrook, *Monopoly, Manipulation, and the Regulation of Futures Markets,* S118, Journal of Business (1986) (''When the closing price on a futures contract significantly diverges from the price of the cash commodity immediately before and after, this is strong evidence that someone has reduced the accuracy of the market price and inflicted real economic loss on participants in the market.'').

[1548] *See* Frank Easterbrook, *Monopoly, Manipulation, and the Regulation of Futures Markets* S124, Journal of Business (1986) (in the specific context of position limits, ''Offenses may be harder to detect when they involve more than one market.'').

[1549] Yiuman Tse & Michael R. Williams, *Does Index Speculation Impact Commodity Prices? An Intraday Analysis,* 48 Financial Review 365–383 (2013).

[1550] Stoll and Whaley also observed that commodity index funds should not be thought of as speculators because they participated in these markets to diversify their returns (relative to equity holdings). In Tse, *The Relationship Among Agricultural Futures, ETFs, and the US Stock Market,* Review of Futures Markets (2012), Tse concluded that there were now positive correlations between agricultural ETF returns and S&P 500. This result suggests that the diversification benefit has at least decreased. In this paper, Tse also found, using 5-minute, intraday returns, that agricultural ETF price returns are Granger-caused by some of the underlying commodity futures market. This result is a rare result finding causation *from* the futures prices *to* financial or institutional traders.

[1551] James W. Williams, *Dodging Dodd-Frank: Excessive Speculation, Commodities Markets, and the Burden of Proof,* 37 Law & Policy 135–38 (2015). (sensitivities of Granger studies to parameters, including time-sensitivity to time intervals, makes ''Granger-inspired studies of excessive speculation . . . problematic,'' a problem compounded by the volatile nature of the commodity markets).

[1552] Dwight R Sanders & Scott H Irwin, *The Impact of Index Funds in Commodity Futures Markets: A Systems Approach,* 14 The Journal of Alternative Investments 40–49 (2011).

[1553] David Frenk, Better Markets, Inc., *Speculation and Financial Fund Activity and The Impact of Index and Swap Funds on Commodity Futures Markets* 6 (2010). Some of Frenk's critiques fall short of the mark. For example, he criticizes Irwin and Sanders for using a one-week interval for their testing. *Id.* at 7. This is not a flaw in the Irwin and Sanders paper and in fact using a one-week time interval helps to ameliorate another problem Frenk identifies: The difficulty of applying Granger analysis to highly volatile data such as commodity prices.

variables.[1554] In a model designed to test whether there is Granger-causation between position changes and price return, additional variables may diminish the statistical power of the position change variable in the testing equation by masking the effect of positon on price returns. The inclusion of these lagged price returns and position change variables in the model design may well diminish the statistical power of the position change variable.[1555] In this way it may also mask a possible correlation between position changes and price returns.[1556]

Other studies doing Granger testing for the effects of commodity index funds on prices arrive at conflicting results.[1557] Then-CFTC economists who were able to access non-public, daily market data to do Granger-based economic analysis of the possible impact of commodity index funds have added to this debate.[1558] A battery of Granger tests discussed in a paper prepared by Bahattin Büyükşahin and Jeffrey H. Harris lead to the conclusion that there was no Granger-causation between swap dealer positions (a proxy for commodity index fund positions) and returns in the crude oil or natural gas futures.[1559] This finding stayed consistent across tests using different time periods within 2000 to 2008 and different lag periods. Rather, Büyükşahin and Harris found price changes Granger-cause changes in position. This study performs an additional Working T analysis and concludes that this measure of speculative positions was not Granger causing price changes in the crude oil or natural gas markets.

The study by Brunetti and Büyükşahin is also an important contribution to the literature.[1560] Brunetti and Büyükşahin consider price returns and positions in several markets (crude oil, natural gas, corn, Eurodollar, and mini-Dow) and find no Granger causation between position and price returns for any of these commodity markets during a time period when commodity index funds were participating in these markets. This study also finds that speculators in these markets during the time period are decreasing, not increasing, volatility.

These CFTC-staff studies have the advantage of using non-public, daily data. However, such studies are subject to the same limitations that are inherent in Granger analysis in this context: The open question of whether the proper time lag was selected, the ad hoc assumption of the time step selected to compute the volatility, and the inclusion in both studies of variables such as lagged price returns that may inadvertently mask correlation. The inherent limitations of Granger analysis may well bear on the conflicting results of these Granger papers.

Agricultural Commodities

The final set of Granger papers concern the agricultural commodity markets. These include a series of papers by Irwin and Sanders and co-authors not finding Granger causation between positions and price returns.[1561] A few papers arrive at nuanced or inconclusive results, but generally cannot find significant Granger causation between position and price in the agricultural commodity markets.[1562]

There are studies (some are more properly categorized as articles) that do purport to find Granger causation between positions and price returns.[1563] The papers finding substantial price impacts caused by speculative positions in the commodity futures markets are not published in academic, peer-reviewed economic or agricultural journals.[1564]

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[1554] Dwight R Sanders & Scott H Irwin, *The Impact of Index Funds in Commodity Futures Markets: A Systems Approach,* 14 The Journal of Alternative Investments 40–49 (2011).

[1555] In Table 54 of the Irwin and Sanders paper, the price return equation used for the Granger correlation analysis diminishes the potential impact of positions on current price returns. Irwin and Sanders use this equation to test for Granger-causation between price returns and position changes, but inclusion of lagged price returns in the equation is problematic. Within the workings of the Granger statistics, placing lagged price returns and change of position data in the same equation can mask the impact of change of positions on price. That is because price returns and lagged price returns may have common correlation; a statistician would say that lagged price return data and change in positions are competing for common correlation with price returns in the Table 4 equation. In this way, the explanatory power of the change in position variable in this Irwin and Sanders paper is diminished by introduction of the lagged price return variables.

[1556] *See* James W. Williams, *Dodging Dodd-Frank: Excessive Speculation, Commodities Markets, and the Burden of Proof,* 37 Law & Policy 137–138 (2015) (Granger methodology may be problematic in analysis of position limits, because there may be nonlinear relationships between economic variables).

[1557] *Compare* Jörg Mayer, United Nations Conference on Trade and Development, *The Growing Interdependence Between Financial and Commodity Markets* (2009).

[1558] Those studies reflect the views of the individual economists, and, not necessarily of the Commission. *Compare* Mayer, *The Growing Interdependence Between Financial and Commodity Markets,* UN Conference on Trade and Development (discussion paper 2009) (finding financial investment in commodity trading Granger-cause price changes in soybeans, soybean oil, copper, crude oilTable 4) *with* IMF Global Financial Stability Report: *Financial Stress and Deleveraging: Macrofinancial Implications and Policy,* Annex 1.2, Financial Investment in Commodities Markets (October 2008) (not providing specifications or background on study, but reporting results finding an absence of Granger causation between position and price in all but the copper markets).

[1559] *See* Bahattin Büyükşahin and Jeffrey H. Harris, *The Role of Speculators in the Crude Oil Futures Market* (working paper 2009).

[1560] Celso Brunetti & Bahattin Buyuksahin, *Is Speculation Destabilizing?,* SSRN Electronic Journal. The Commission cited this study in particular in its December 2013 Position Limits Proposal. *See also* Letter from CME Group, Inc., to CFTC (Mar. 28, 2011).

[1561] *See, e.g.,*Irwin and Sanders, *The ''Necessity'' of New Position Limits in Agricultural Futures Markets: The Verdict from Daily Firm-Level Position Data* (working paper 2014); Irwin and Sanders, *The Performance of CBOT Corn, Soybean, and Wheat Futures Contracts after Recent Changes in Speculative Limits* (working paper 2007); Sanders, Irwin, and Merrin, *Smart Money? The Forecasting Ability of CFTC Large Traders,* Journal of Agricultural and Resource Economics (2009); Sanders, Irwin, and Merrin, *A Speculative Bubble in Commodity Futures? Cross-Sectional Evidence,* Agricultural Economics (2010); Irwin, Sanders, and Merrin, *Devil or Angel: The Role of Speculation in the Recent Commodity Price Boom,* Journal of Agricultural and Applied Economics (2009); Sanders, Irwin, and Merrin, *The Adequacy of Speculation in Agricultural Futures Markets: Too Much of a Good Thing?,* Applied Economic Perspectives and Policy (2010). An additional paper is, for the most part, in accord with Irwin and Sanders' work. Aulerich, Irwin, and Garcia, *Bubbles, Food Prices, and Speculation: Evidence from the CFTC's Daily Large Trader Data Files* (NBER Conference 2012) (concluding overall that buying pressure from financial index investment in recent years did not cause massive price ''bubbles'' in agricultural futures prices, and any such evidence of price increase is weak evidence of small and fleeting price impact).

[1562] *See, e.g.,* Borin and Di Nino, *The Role of Financial Investments in Agricultural Commodity Derivatives Markets* (working paper 2012) (finding ''sparse'' evidence of Granger causation between traders' investment decisions and futures prices and also ''scarce evidence of hearing behavior except in the cotton market''); Grosche, *Limitations of Granger Causality Analysis to Assess the Price Effects From the Financialization of Agricultural Commodity Markets Under Bounded Rationality,* Agricultural and Resource Economics (2012); Gilbert, *How to Understand High Food Prices,* Journal of Agricultural Economics (2008); Robles, Torero, and von Braun, *When Speculation Matters* (working paper 2009) (speculative trading may have influenced agricultural commodity prices ''but the evidence is far from conclusive'').

[1563] *See, e.g.,* Algieri, *Price Volatility, Speculation and Excessive Speculation in Commodity Markets: Sheep or Shepherd Behaviour?* (working paper 2012) (''excessive speculation'' has driven price volatility for maize, rice, soybeans, and wheat for a particular timeframe); Cooke and Robles, *Recent Food Prices Movements: A Time Series Analysis* (working paper 2009) (concluding that financial activity in futures market and proxies for speculation can help explain observed changes in international food prices for corn, wheat, rice, and soybeans); Timmer, *Did Speculation Affect World Rice Prices?,* UN Food and Agricultural Organization (working paper 2009) (concluding that the price of rice was not affected by financial speculators, but run-ups in wheat and corn prices ''was almost certainly caused by financial speculators''); Varadi, *An Evidence of Speculation in Indian Commodity Markets* (working paper 2012) (inferring the unexplained price increases must be due to speculation).

[1564] Other limitations arise from fairly cryptic inferential reasoning that the cause of any price-run

Continued

Gilbert, in a 2008 paper, reaches a different result with respect to agricultural commodities.[1565] Gilbert performs Granger testing on other variables that could explain (in the sense of Granger-causing) run-ups in agricultural commodity futures prices. Specifically, he looks at macroeconomic and financial factors that affected the price of many commodities during the 2005–2008 time period.[1566] Gilbert obtains results suggesting that the main determinants in agricultural commodity futures prices during this time period are macroeconomic (such as GDP growth) and financial factors (such as the value of the dollar and interest rates).[1567] Gilbert concludes that (1) there is little Granger-causation evidence that speculation by commodity index funds caused the run-up in agricultural commodity prices during this time period; and (2) moreover, there is evidence that macroeconomic factors other than ''excessive speculation'' might have caused the price run-up. Gilbert's work does not purport to show that macroeconomic and financial factors account for all price changes. Moreover, his 2008 piece is difficult to reconcile with his 2010 work, which does find price impacts from speculation using Granger analysis for some agricultural commodities.[1568]

The work of Gilbert, as well as Irwin and Sanders, also suggest a cautious approach is warranted in concluding how sizeable or lasting any price impact associated with ''excessive speculation'' can be, at least when employing a Granger analysis. One paper authored by Irwin emphasized that the only evidence of Granger-causation between positions and price returns in the agricultural market was weak evidence of temporary changes in price.[1569]

The debate is hard to resolve, including for the fairly technical reasons provided in Grosche.[1570] Grosche observes that index trading and other financial investment may be based on a mixture of speculative and hedging motives in the agricultural sphere.[1571] The interaction between the physical and financial contracts in the agricultural commodity sphere is under-researched and the possible ''spillover'' effects from financial to agricultural markets is unknown.[1572]

b. Comovement, Cointegration and ''Financialization''

i. Description

These studies employ a statistical method that can be viewed mathematically as a special case of Granger causality, a method frequently referred to as comovement. This method looks for whether there is correlation that is contemporaneous and not lagged. (This is effectively similar to a Granger analysis where the type period of lag is set to zero.) Like Granger causality, this method employs linear regression to establish correlation between market prices or price returns and speculative positions. When the time step is set to zero, the economist can no longer seek to establish an inference of cause and effect between prices or price returns and positions. Instead, the economist is using a Granger-type analysis to establish whether there is a correlation that is contemporaneous. A subset of these comovement studies uses a technique called cointegration for testing correlation between two sets of data, to see if there is a statistical relationship notwithstanding the ''white noise'' of price data.[1573]

This technique can be used to ferret out unexpected divergences in prices. For example, many economists perform cointegration tests comparing futures and spot prices, which generally should constrain each other by staying within reasonable bands of each other. If they find a discrepancy, they consider whether excess speculation or a price ''bubble'' could explain this price discrepancy.

ii. Advantages and Disadvantages

Such approaches are useful to compare commodity markets with other markets in seeking a correlation over time between these sets of prices. For example, a study may look at a price index for commodities for one time series and a price index for equities for another time series. In rough terms, studying the linear regressions of these price data over time establishes whether there is a confluence of price trends in these two markets. It may capture correlations that a Granger causality approach may miss if the latter uses too large a time lag. In this way, comovement analyses may be stronger than Granger analyses at finding correlations, avoiding the problem of correlations being hidden by the improper selection of length of time lag.

But the complementary disadvantage is that a comovement result cannot establish even weak, Granger-style causation. In the particular context of position limits, this disadvantage is significant. As further explained below in the discussion of specific studies, correlations between prices or price returns and positions can be caused by external factors such as broad macroeconomic trends. In particular, using comovement to try to establish a ''price bubble'' over time ranges that are short-term (months) or medium-term (18 months to two years) is problematic because of the impact macroeconomic or other external factors (wars, recessions, etc.) can have on short-term prices. A comovement study showing a correlation between two sets of data—crude oil futures and spot prices—over just a year or two years is, all else being equal, a fairly weak basis to infer a price bubble. There can be other factors that cause decoupling of prices over such a time period.

iii. ''Financialization''

Many of the papers in this category focus on a documented correlation between returns to commodity futures and the financial (including equity) markets that has increased strongly in

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up must be due to speculation. *See, e.g.,* Timmer, *Did Speculation Affect World Rice Prices?,* 38, UN Food and Agricultural Organization (working paper 2009) (regarding theory that financial speculators are the cause for price run-ups, the paper states that ''[t]hese conclusions are reached mostly by eliminating the other explanations and by logical reasoning''); Varadi, *An Evidence of Speculation in Indian Commodity Markets* (working paper 2012) (asserting author's ''estimations'' that speculation has played a ''decisive role'' in creating commodity price bubbles in Indian commodity markets, without provision of a theoretical framework to reach this conclusion).

[1565] Christopher J. Gilbert, *How to Understand High Food Prices,* Journal of Agricultural Economics (2008).

[1566] *Id.*

[1567] *Id.* at 27–28.

[1568] Gilbert, *Speculative Influences on Commodity Futures Prices, 2006–2008,* 24 (Table 4), UN Conference on Trade and Development (2010) (referencing price impacts in wheat, corn, and soybean).

[1569] Aulerich, Irwin, and Garcia, *Bubbles, Food Prices, and Speculation: Evidence from the CFTC's Daily Large Trader Data Files,* 22 (NBER Conference 2012) (finding some weak evidence of temporary changes in price Granger-caused by positions, but observing that the ''size of the estimated system impact is too small'' to be consistent with the commodity index funds causing a huge run-up in prices).

[1570] Grosche, *Limitations of Granger Causality Analysis to Assess the Price Effects from the Financialization of Agricultural Commodity Markets Under Bounded Rationality,* Agricultural and Resource Economics (2012).

[1571] *Id.* at 18.

[1572] *Id.* at 17. *See also* Williams, *Dodging Dodd-Frank: Excessive Speculation, Commodities Markets, and the Burden of Proof,* Law & Policy Journal of the University of Denver (2015).

[1573] Two time series of price data are said to be cointegrated if the error term in the modeling of their statistical correlation is a term that is, among other things, independent of time. In layperson's terms, the two streams of price data each roughly follow a random walk through time. (In more technical terms, cointegration means there is a linear connection between the two streams of data where the difference is ''white noise'' (Brownian motion) or a random walk. There is some cointegrating vector of coefficients that can be used to form a linear combination of the two time series.)

recent years.[1574] This is often called comovement between the commodity and financial markets. The many factors that have driven explosive growth in commodity derivatives trading in recent years are well-documented in a study by Basu and Gavin.[1575] There has been substantial growth in commodity index investments; this includes commodity exchange-traded funds and other commodity indices that fund managers and other financial investors use. Both the number of such indices, and the volume of trading involving them, has grown substantially in the last decade. There have also been significant changes in the long positions held in commodity futures index funds during the financial crisis:[1576]

**Notional Long Positions Invested in Commodity Futures Index Funds**

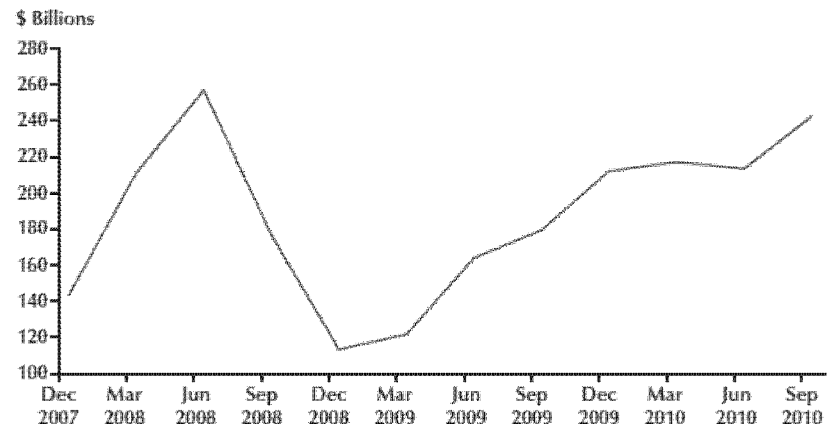
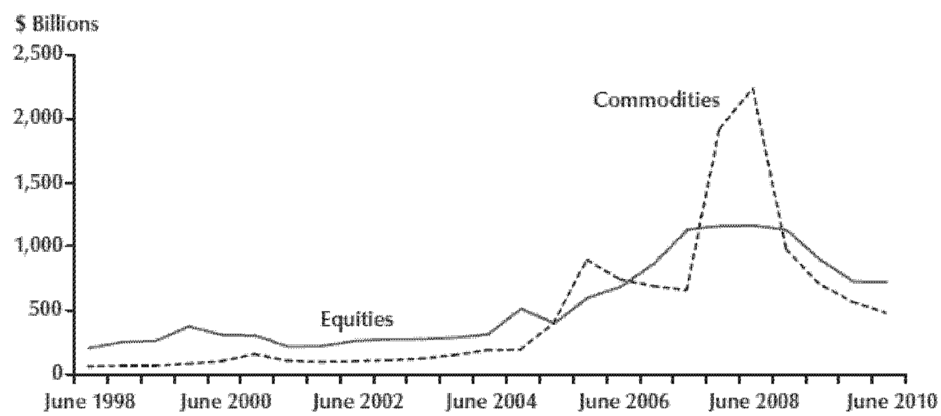



Figure 1B. Over-the-counter trading in commodity derivatives by swap dealers has also increased over time, with a pronounced spike during the 2007–2008 time period.[1577]

**OTC Trading in Commodity and Equity Derivatives (gross market value)**




SOURCE: Bank for International Settlements derivatives statistics.

Figure 2B. The factors driving this growth include the desire of institutional portfolio managers to hedge against stock risk, based on the belief by some academic and industry economics that there were negative correlations between returns on equity and commodity futures.[1578] This belief may not be economically justifiable.[1579] Investors also sought higher yields in a low-yield environment.[1580]

[1574] Tang and Xiong, *Index Investment and Financialization of Commodities,* Financial Analysts Journal (2012).

[1575] Basu and Gavin, *What Explains the Growth in Commodity Derivatives?,* Federal Reserve Bank of St. Louis (2011).

[1576] *Id.* at 40.

[1577] *Id.* at 41.

[1578] *Id.* at 38, 44–45.

[1579] *See id.* at 44 (however, following the collapse of commodity prices in the summer of 2008 and subsequent financial panic in September of 2008, the correlation between commodity prices and equities became highly and positively correlated). Use of commodities to hedge equity or business cycle risk is controversial. Basu and Gavin, *What Explains the Growth in Commodity Derivatives?,* at 44 Federal Reserve Bank of St. Louis (2011), *citing* Büyükşahin, Haigh, and Robe (2008) (unconditional correlation between equity and commodity futures returns is near zero).

[1580] *Id.* at 38, 44.

iv. The Masters Hypothesis

One variation on this financialization theme is the Masters ''hypothesis.'' Michael W. Masters, a hedge fund manager, is a leading proponent of the view that commodity index investments have been a major driver of increases in the commodity futures prices. In brief, his views are expressed in the following statement:

> Institutional Investors, with nearly $30 trillion in assets under management, have decided en masse to embrace commodities futures as an investable asset class. In the last five years, they have poured hundreds of billions of dollars into the commodities futures markets, a large fraction of which has gone into energy futures. While individually these Investors are trying to do the right thing for their portfolios (and stakeholders), they are unaware that collectively they are having a massive impact on the futures markets that makes the Hunt brothers pale in comparison. In the last 4½, years assets allocated to commodity index replication trading strategies have grown from $13 billion in 2003 to $317 billion in July 2008. At the same time, the prices for the 25 commodities that make up these indices have risen by an average of over 200%. Today's commodities futures markets are excessively speculative. . . .[1581]

Statements are not, in themselves, rigorous economic studies, nor do they purport to be. Several economists have attempted to formalize and study rigorously the ''Masters hypothesis'' or related conjectures using comovement or cointegration methods. These studies are discussed below.

v. Discussion of Specific Studies

There are 25 papers that use some form of comovement or cointegration analysis, broadly defined. Former and current economists within the Office of Chief Economist have used this method repeatedly (7 papers); [1582] several government and policy researchers deploy this method (4 papers); [1583] and other academicians have used this method (14 papers).[1584]

The Example of Oil Prices 2006–2008

One of the key challenges for application of the Masters hypothesis is reconciliation of a supposed speculative price with what is happening in the physical market. The debate within academia, practitioners and policymakers on this topic has been considerable, especially given the run-up in prices in certain commodities, such as the 2006–2008 rise in crude oil prices. ''Dramatic swings in crude oil prices have led Congress to examine the functioning of the markets where prices are set.'' [1585] The correlation of oil with economic trends is not necessarily evidence that they are causing increases in oil prices. As a Congressional Research Study observed, this might suggest that certain traders with ''better information on macroeconomic trends, which strongly influence energy demand, take more aggressive positions, which would then influence oil prices.'' [1586]

The economics of the crude oil market are a good example of the dangers of applying comovement or cointegration methods over short- and medium-term. Short-term crude oil prices are less elastic than longer-term prices. This means, in the short term, changes in price do not affect the supply of crude oil as much as long-term price changes do. There are many reasons why this is so, having to do with the cost of storing crude oil above ground and the cost of starting and stopping crude oil extraction. So it is unsurprising that there are short- and medium-term divergences in price between spot and longer-term futures contracts in the crude oil markets.

On the supply side of crude oil market economics, a short-term shock to supply (wars, embargoes, or other events) will not necessarily translate into a long-term change in prices, even though it may cause substantial short-term price changes and volatility. Similarly, on the demand side of crude oil market economics, short-term changes to demand can impact short-term crude oil prices without causing lasting long-term price impact.[1587]

For such reasons, comovement and cointegration studies of crude oil prices over medium time frames are unpersuasive.[1588] Büyükşahin and Robe showed that correlations between equity and energy commodity investments increased massively after Lehman's

[1581] M.W. Masters, A.K. White, *The Accidental Hunt brothers: How Institutional Investors Are Driving up Food and Energy Prices, www.accidentalhuntbrothers.com* (2008). Mr. Masters, Portfolio Manager for Masters Capital Management, LLC, has often referred to these large investors as ''passive'' investors. ''Passive speculators are an invasive species that will continue to damage the markets until they eradicated.'' Masters Statement, CFTC March 2010 hearing at 5. According to Barclay's, index fund investment fund in commodities reached $431 billion as of July 2011. Algieri, *A Roller Coaster Ride,* 5 (working paper 2011).

[1582] *See, e.g.,* Boyd, Büyükşahin, and Haigh, *The Prevalence, Sources, and Effects of Herding* (working paper 2013); Büyükşahin and Robe, *Does it Matter Who Trades Energy Derivatives?,* Review of Env't, Energy, and Economics (2013); Büyükşahin and Robe, *Speculators, Commodities, and Cross-Market Linkages* (working paper 2012); Büyükşahin and Robe, *Does ''Paper Oil'' Matter?* (working paper 2011); Büyükşahin, Harris, and Haigh, *Fundamentals, Trader Activity, and Derivatives Pricing* (working paper 2008); Cheng, Kirilenko, and Xiong, *Convective Risk Flows in Commodity Futures Markets* (working paper 2012); and Haigh, Harris, and Overdahl, *Market Growth, Trader Participation and Pricing in Energy Futures Markets (*working paper 2007).

[1583] *See, e.g.,* Baffes and Haniotos, *Placing the 2006/08 Commodity Boom into Perspective,* World Bank Policy Research Working Paper 5371 (2010); Belke, Bordon, and Volz, *Effects of Global Liquidity on Commodity and Food Prices,* German Institute for Economic Research (2013); Kawamoto, Kimura, et al., *What Has Caused the Surge in Global Commodity Prices and Strengthened Cross-market Linkage?,* Bank of Japan Working Papers Series No.11–E–3 (May 2011); and Pollin and Heintz, *How Wall Street Speculation is Driving Up Gasoline Prices Today* (AFR working paper 2011).

[1584] *See, e.g.,* Adämmer, Bohl and Stephan, *Speculative Bubbles in Agricultural Prices* (working paper 2011); Algieri, A Roller Coaster Ride: An Empirical Investigation of the Main Drivers of Wheat Price (working paper 2013); Babula and Rothenberg, *A Dynamic Monthly Model of U.S. Pork Product Markets: Testing for and Discerning the Role of Hedging on Pork-Related Food Costs,* Journal of Int'l Agricultural Trade and Development (2013); Basu and Miffre, *Capturing the Risk Premium of Commodity Futures: The Role of Hedging Pressure,* Journal of Banking and Risk (2013); Hoff, Herding Behavior in Asset Markets, Journal of Financial Stability (2009); Tang and Xiong, *Index Investment and Financialization of Commodities,* Financial Analysts Journal (2012); Creti, Joets, and Mignon, *On the Links Between Stock and Commodity Markets' Volatility,* Energy Economics (2010); Bichetti and Maystre, *The Synchronized and Long-lasting Structural Change on Commodity Markets: Evidence from High Frequency Data* (working paper 2012); Bunn, Chevalier, and Le Pen, *Fundamental and Financial Influences on the Co-movement of Oil and Gas Prices* (working paper 2012); Coleman and Dark, *Economic Significance of Non-Hedger Investment in Commodity Markets* (working paper 2012); Dorfman and Karali, *Have Commodity Index Funds Increased Price Linkages between Commodities?* (working paper 2012); Korniotis, *Does Speculation Affect Spot Price Levels? The Case of Metals With and Without Futures Markets* (working paper, FRB Finance and Economic Discussion Series 2009) (*also submitted as a comment by CME*); Le Pen and Sévi, *Futures Trading and the Excess Comovement of Commodity Prices* (working paper 2012); and Windawi, *Speculation, Embedding, and Food Prices: A Cointegration Analysis* (working paper 2012).

[1585] Jickling and Austin, *Hedge Fund Speculation and Oil Prices* 1 (Congressional Research Service R41902 June 29, 2011).

[1586] *Id.* at 16, (Congressional Research Service R41902 June 29, 2011).

[1587] This is true for a variety of reasons, including the fact that refining production is expensive to change on short notice. *See generally* Hamilton, Causes and Consequences of the Oil Shock of 2007–2008, at 17–23, Brookings Paper on Economic Activity (2009) (while oil prices may have been ''too high'' in July 2009, ''low price elasticity of demand, and the failure of physical production to increase'' are more likely the predominant causes than ''speculation per se'').

[1588] Pollin and Heintz, How Wall Street Speculation is Driving Up Gasoline Prices Today, at 10, Americans for Financial Reform (working paper 2011) (''Lagged values of both gasoline prices and crude oil prices can affect current gas prices. This implies that past speculative pressures are carried over, at least for several months, to current prices.''); Bunn, Chevalier, Le Pen, and Sevi, Fundamental and Financial Influences on the Co-movement of Oil and Gas Prices, at 18 (working paper 2012) (''we find significant evidence that speculation, with its focus on index trading, increases the correlation between oil and gas'').

collapse in 2008.[1589] As explained in another paper by Büyükşahin and Robe, this raises the question of whether hedge fund and index fund inflows are transmitting financial shocks to commodity prices.[1590] However, as Büyükşahin and Robe's survey of Granger and comovement economic literature demonstrate, it does not appear that index traders and hedge funds had an impact on crude oil prices during this time period.[1591] Further, Celso Brunetti and Bahattin Büyükşahin separately found that hedge funds exert a calming influence on crude oil prices by lowering oil price volatility.[1592]

Cointegration results suggest that financial traders' influence of crude oil futures prices is desirable. For example, then-CFTC economists, Büyükşahin, Harris, and Haigh show how the increased presence of swap dealers, hedge funds, and other financial traders have led to the cointegration of various crude oil futures contracts (the nearby contract, the one-year contract, and the two-year contract).[1593] This co-integration result by these economists suggests that there was a long-term relation between the strength of price cointegration and the market activities of financial traders,[1594] but this result does not suggest any harm to the marketplace or price discovery from the cointegration of various crude oil contracts. The authors conjecture that the greater market activity by these traders can ''enhance market quality'' through ''enhance[d] linkages among various futures prices'' that make these commodity markets ''more informationally efficient.'' [1595]

Both research papers [1596] are correct that, respectively, there is increased comovement between crude oil prices with financial investments and cointegration between nearby, one-year, and two-year crude oil futures contracts. At least for the crude oil market, these price linkages exist. However, one cannot obtain, using comovement and cointegration techniques, decisive evidence on whether this effect improves market efficiency; such a conclusion involves interpreting the informational linkages between the markets. To the extent that the paper by Büyükşahin, Harris, and Haigh moves beyond establishing the linkage to inferring that the linkage has salutary effects on commodity markets, that conclusion was not empirically tested, because it was not modelled explicitly. At most, these studies establish the existence of such price linkages.

Financialization Comovement Literature

Some studies have examined ''financialization'' by using comovement analysis to ask whether increased investment flows into commodity indices (typically composed with substantial long futures positions) are correlated with increases in futures prices or the volatility of commodity futures prices across many different types of studies. Some of these financializaton comovement studies have looked to whether these investment flows decrease the risk premium for holding a long futures contract, thereby causing a non-transient increase in the long futures contract price (which, in turn, may increase the price of the underlying commodity).

There is consensus in the economic literature that equities and commodities no longer exhibit the strong negative correlations that index fund investment managers may have sought in hedging their portfolios. In recent years there has been an increased positive correlation between equity and commodity prices since 2008.[1597] There is also substantial consensus among economists who study this issue that risk premiums for holding long futures contracts have decreased due to financialization.[1598]

However, there is a divergence of views among economists on the impacts, if any, on the large positions taken by index funds on commodity futures prices or price volatility.[1599] These hypothesized effects of financialization are debated among academics, practitioners, and policymakers. Results of studies that test for a bubble component in commodity futures prices—regardless of the cause—are decidedly mixed.[1600]

Commission-affiliated economists have confirmed a general decrease in volatility associated with financialization, a salutary effect associated with increased liquidity.[1601] In theoretical models outside the comovement methodology, competition from index investment reduces the risk premium that accrues to long position holders, and this can have the net effect of lowering the cost of hedging to traditional physical market participants.[1602] Some economists rely upon the efficient market hypothesis that market prices fully incorporate all the available public ''information'' into prices—in support of conclusion that financialization provides benefits such as better price discovery, liquidity, and transfer of risks to entities better

[1589] Büyükşahin and Robe, *Does ''Paper Oil'' Matter?* (working paper 2011).

[1590] Büyükşahin and Robe, *Does it Matter Who Trades Energy Derivatives?,* Review of Env't, Energy, and Economics (2013).

[1591] *Id.* at 5.

[1592] Celso Brunetti and Bahattin Büyükşahin, *Is Speculation Destabilizing?* (working paper 2009). *See also* Haigh, Harris, and Overdahl, Market Growth, Trader Participation and Pricing in Energy Futures Markets (working paper 2007) (participation of swap dealers and arbitrageurs has assisted in improved price efficiency—price converge—in crude oil futures contracts, with nearby, one, and two-year crude oil futures contracts statistically cointegrated through the period studied, July 2004 to mid-2006).

[1593] Büyükşahin, Harris, and Haigh, *Fundamentals, Trader Activity, and Derivatives Pricing* (working paper 2008).

[1594] *Id.* at 3.

[1595] *Id.* at 4–5.

[1596] Büyükşahin and Robe, *Does it Matter Who Trades Energy Derivatives?,* Review of Env't, Energy, and Economics (2013); Büyükşahin, Harris, and Haigh, *Fundamentals, Trader Activity, and Derivatives Pricing* (working paper 2008).

[1597] *E.g.,* Basu and Gavin, What Explains the Growth in Commodity Derivatives?, at 44 Federal Reserve Bank of St. Louis (2011) (commodity and equity prices highly and positively correlated in February 2010); Tang and Xiong, Index Investment and Financialization of Commodities, Financial Analysts Journal (2012); Inamura, Kimata, et al., Recent Surge in Global Commodity Prices (Bank of Japan Review March 2011).

[1598] Hamilton and Wu, Risk Premia in Crude Oil Futures Prices, Journal of International Money and Finance (2013).

[1599] *See* Irwin and Sanders, *Index Funds, Financialization, and Commodity Futures Markets,* at 15, Applied Economic Perspectives and Policy (2010) (surveying literature in support and against the idea of a speculative bubble in prices arising from commodity index fund participation in the futures market). *Compare* Gilbert, *Speculative Influences on Commodity Futures Prices,* 2006–2008, UN Conf. On Trade Development (2010); Einloth, *Speculation and Recent Volatility in the Price of Oil* (working paper 2009), and Tang and Xiong, *Index Investment and Financialization of Commodities,* Financial Analysts Journal (2012) *with* Bahattin Büyükşahin and Jeffrey H. Harris, *The Role of Speculators in the Crude Oil Futures Market* (working paper 2009); Brunetti and Büyükşahin, *Is Speculation Destabilizing?* (working paper 2009); Stoll and Whaley, *Commodity index Investing and Commodity Futures Prices,* Journal of Applied Finance (2010), Irwin and Sanders (multiple studies).

[1600] *See, e.g.,* Büyükşahin and Robe*, Speculators, Commodities, and Cross-Market Linkages* (working paper 2012); Irwin and Sanders, *Index Funds, Financialization, and Commodity Futures Markets,* at 15, Applied Economic Perspectives and Policy (2010), *citing, inter alia,* Phillips and Yu, *Dating the Timeline of Financial Bubbles During the Subprime Crisis,* Quantitative Economics (2011); and Kilian and Murphy, *The Role of Inventories and Speculative Trading in the Global Market for Crude Oil,* Journal of Applied Econometrics (2010).

[1601] Brunetti and Büyükşahin, *Is Speculation Destabilizing?* (working paper 2009) (finding that hedge funds in the commodity markets take the opposite position to other market participants, therefore providing liquidity to the market in various commodity market places studied, including crude oil, natural gas, corn, and two financial contracts).

[1602] Acharya, Ramadorai, and Lochstoer, *Limits to Arbitrage and Hedging: Evidence from Commodity Markets,* Journal of Financial Economics (2013) (existence of financial commodity index trading will tend to decrease risk premium, thereby generally making it cheaper for producers to hedge through short futures contracts).

prepared to assume it.[1603] Comovement and cointegration analyses are some of the statistical tools used to test whether these purported benefits of greater market participation hold true under particular market conditions.

While competition and increased trading volume can generally help markets, inflows do not universally benefit market welfare. In a paper by Cheng, Kirilenko, and Xiong, the authors use comovement methodology to conclude that in times of distress, financial traders reduce their net long position, causing risk to flow from financial traders to commercial hedgers.[1604] ''[J]ust when the uncertainty in the economy was rising, the number of futures contracts used by commercial hedgers to hedge their risk was going down.'' [1605]

Cheng, Kirilenko, and Xiong argue that tests such as Granger, which look to whether financial traders' positions and futures prices are negatively correlated when they trade to accommodate hedgers, overlook an important lesson from the distressed financial literature.[1606] When financial entities trade in response to their own financial distress, their trades may be correlated positively to futures price changes. These correlations may net out, so that any significant correlation between their positions and price changes may be masked by trading during financial distress.[1607]

Using cointegration techniques and non-public trading data, then-CFTC economists, Büyükşahin and Robe demonstrate that the correlations between equity indices and commodities increase with greater participation by financial speculators.[1608] There is no such effect for other types of traders. In concert with the work of Cheng, Kirilenko, and Xiong, they find that this cointegration effect, the price linkages between equity indices and investible commodities, is lower during times market stress.

Another comovement study provided an empirical link between commodity index investment and futures price movements, including increased price volatility.[1609] Tang and Xiong find that the increasing presence of index traders in commodity futures markets improves risk sharing in these markets with concomitant volatility spillover from outside markets. This study finds evidence of volatility spillovers from the financial crisis in the 2006–2009 time period, spillovers that may have been a key driver of recent commodity price volatility.[1610]

This Tang and Xiong finding of volatility ''spillovers'' is frequently cited by commenters in support of position limits. However, some academics are skeptical of their results. Irwin and Sanders concede that the Tang and Xiong paper ''appears to offer concrete evidence'' of some form of financialization, but offers several reasons to view these findings with caution.[1611]

Tang and Xiong's results do not necessarily point to lasting difficulties associated with the integration of financial and commodity markets. Instead, they argue that commodity markets were not integrated with financial markets prior to the development of commodity index funds. In their paper, Tang and Xiong view financialization as a ''process'' which helps explain ''the synchronized price boom and bust of a broad set of seemingly unrelated commodities'' during the 2006–2008 time period.[1612]

A problem with this line of reasoning that critics have identified is that there could be other factors which lead to increased correlation between equities and futures during this time period. After all, 2006–2009 was an eventful time where broad macroeconomic factors held sway and could have led to large positive correlations between these markets. According to many, one of the factors leading to the influx of investment funds in during the 2006–2008 time period was negative correlations between commodities returns and equities returns. Yet this factor is less prevalent today. ''The positive correlation between the agriculture ETFs and S&P 500 suggests that the diversification benefits of using an agricultural index have decreased.'' [1613]

Some commenters have pointed to studies such as Tang and Xiong's in support of the position limits rule.[1614] However, most financial investors' exposure to commodities through commodity index funds or ETFs would not be prevented by position limits. Studies on the price returns or price volatility effect of commodity index funds are thus not directly relevant to the placement of position limits on individual commodities contract.[1615] Moreover, commodity index funds are not the only large investors whose activities may affect commodity futures prices.[1616]

A paper by Korniotis contains an important caveat in the financialization debate: The effects of financialization may vary widely depending on the type of commodity.[1617] Crude oil is an important component of the S&P Goldman-Sachs Commodity Index

[1603] Filimonov, Bicchetti, and Maystre, Quantification of the High Level of Endogeneity and of Structural Regime Shifts in Commodity Markets, at3 and citations therein (working paper 2013).

[1604] Cheng, Kirilenko, and Xiong, *Convective Risk Flows in Commodity Futures Markets* (working paper 2012).

[1605] Id. at 2 (citing papers on a growing body of theoretical work indicating that at times of financial crisis, funding and risk constraints may force financial traders to unwind positions, which, in turn, forces hedgers to reduce their hedging positions).

[1606] *Id.* at 3.

[1607] *Id. See also* Acharya, Ramadorai, and Lochstoer, *Limits to Arbitrage and Hedging: Evidence from the Commodity Markets,* Journal of Financial Economics (2013) (decreases in financial traders' risk capacity should lead to increases in hedgers' hedging cost, all else being equal).

[1608] Büyükşahin and Robe, *Speculators, Commodities, and Cross-Market Linkages* (working paper 2012).

[1609] Tang and Xiong, *Index Investment and Financialization of Commodities,* Financial Analysts Journal (2012).

[1610] Of course, the spillover effect may not be limited to domestic markets. Cf. UN Food and Agricultural Org., Price Volatility in Agricultural Markets. Economic and Social Perspectives Policy Brief 12 (2010) (citing financialization as a possible basis for short-term volatility and observing that international integration of markets can propagate price risks to domestic markets quicker than before).

[1611] Irwin and Sanders, *Index Funds, Financialization, and Commodity Futures Markets,* 15, Applied Economic Perspectives and Policy (2010) (questioning the small magnitude of correlation and suggesting that Tang and Xiong may not have adequately controlled for fundamental factors affecting price).

[1612] Tang and Xiong, *Index Investment and Financialization of Commodities,* Financial Analysts Journal (2012).

[1613] Tse, *The Relationship Among Agricultural Futures, EFTs, and the US Stock Market,* at 16, Review of Futures Markets (2012). Indeed, this decreased correlation may be due, in part, to ethanol, an economic substitute for gasoline as an additive to reformulated blend stock, being manufactured with corn and other grains.

[1614] *See generally* Henn Letter.

[1615] *See* December 2013 Position Limits Proposal at 75740 n.483 (''The speculative position limits that the Commission proposes apply only to transactions involving one commodity or the spread between two commodities . . . . They do not apply to diversified commodity index contracts involving more than two commodities . . . . [C]ommenters assert that such contracts, which this proposal does not address, consume liquidity and damage the price discovery function of the marketplace'').

[1616] Irwin and Sanders, *Index Funds, Financialization, and Commodity Futures Markets,* at 26, Applied Economic Perspectives and Policy (2010) (emergency evidence that ''other traders, such as broker-dealers and hedge funds, play key roles in transmitting shocks to commodity futures markets from other sectors''), *citing, inter alia* Büyükşahin and Robe, *Does it Matter Who Trades Energy Derivatives?,* Review of Env't, Energy, and Economics (2013); Haigh, Hranaiova, and Overdahl, *Hedge Funds, Volatility, and Liquidity Provisions in the Energy Futures Markets,* Journal of Alternative Investments (Spring 2007); Basu and Gavin, *What Explains the Growth in Commodity Derivatives?,* Federal Reserve Bank of St. Louis (2011) (documenting increased participation in commodity trading by swap dealers).

[1617] Korniotis, *Does Speculation Affect Spot Price Levels? The Case of Metals With and Without Futures Markets* (working paper, FRB Finance and Economic Discussion Series 2009).

(GSCI), more so than industrial metals. Federal Reserve Board economist George Korniotis found that there was cointegration between metals with and without futures contracts that did not weaken as financial speculation increased in the marketplace and the spot prices for industrial metals were unrelated to the GSCI.

With the exceptions discussed in detail above, many of the studies in this vein do not warrant detailed discussion. Even well-executed economic studies using comovement methodology that do not focus on position limits may be of little or marginal relevance.[1618]

Herding

There are other possible ways in which additional trading volume may not be an unalloyed benefit to the wellbeing of a marketplace. A few comovement studies attempt to test for the existence of ''herding.'' This is a formalized version of price trending. The idea here is that traders may initiate a trade with the expectation that positive-feedback traders will purchase the traded instruments at a higher price later.[1619] Some economists argue that financialization aggravates ''herding'' behavior and herding creates price bubbles.[1620] Others dispute any such effect.[1621]

Though the evidence for herding is meager, the underlying idea is consistent with accepted and theoretically plausible results on risk premia. Risk premiums rise with the volatility of the futures markets, and risk premiums depend in part on speculators' hedging pressure and inventory levels.[1622]

Agricultural Commodities and Financialization

Agricultural economists have reached similarly conclusions on the cointegration of financial speculators and food prices. While there are respectable empirical results suggesting that financial speculation have affected some recent agricultural commodity price dynamics, there is no unanimity in the academic community on conclusive empirical evidence of the causal dynamics, breadth, and magnitude of such effects.[1623]

c. Models of Fundamental Supply and Demand and Related Methods

i. Description

Some economists have developed economic models for the supply and demand of a commodity. These models often include theories of how storage capacity and use affect supply and demand, often a critical factor in the case of physical commodities and their inter-temporal price (that is, their price over time). Using models of supply and demand, the economists then attempt to arrive at a ''fundamental'' price (or price return) for commodity based on the model. Specifically, the economists look at where the model is in equilibrium with respect to quantities supplied and quantities demanded to arrive at this price. The fundamental price given by such a model is then compared with actual prices. The economists look for deviations between the fundamental price, based on the model, and the actual price of the commodity. When pursuing this method, economists look for whether the price deviations are statistically significant. When there are statistically significant deviations of the actual price from market fundamentals, they infer that the price is not driven by market fundamentals.

Many of these studies present a model for one particular commodity or set of commodities. Some looked at volatile markets. Others used at very predictable markets.

We group together for analysis a diverse set of studies that fall within this broad category of economic models of fundamental supply and demand. Some asserted that their models generally could explain prices. Some papers were neutral. And some papers reached the conclusion that market fundamentals could not explain certain price data in the markets they studied.

ii. Advantages

This methodology is well-recognized and accepted means for detecting price deviations. This is a centuries-old technique, as old as the quantification of economics. The model forces the economist to explain supply and demand. This requirement thus provides welcome transparency.

Moreover, the models are auditable: When the fundamental price deviates from the actual price, the economists may well be able to look at the model and see which aspects of supply and/or demand created the deviation. If the economist cannot ascertain the source of the deviation, (1) the economist may seek to add additional variables to the models for supply or demand to better model supply and demand or (2) conclude that this unexplained deviation is empirical support for the existence of a non-fundamental price.

Another advantage of this model is that the loose language of ''bubble'' is replaced by the term ''non-fundamental price.'' The model supplies an economically motivated specification for the price of a commodity. This feature permits deeper economic analysis and debate on whether a non-fundamental price exists without a digression into debates about what the term ''bubble'' means.[1624]

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[1618] *See* Baffes and Haniotos, *Placing the 2006/08 Commodity Boom into Perspective,* World Bank Policy Research Working Paper 5371 (2010); Kawamoto, Kimura, et al., *What Has Caused the Surge in Global Commodity Prices and Strengthened Cross-market Linkage?,* Bank of Japan Working Papers Series No.11–E–3 (May 2011); Coleman and Dark, *Economic Significance of Non-Hedger Investment in Commodity Markets* (working paper 2012); Dorfman and Karali, *Have Commodity Index Funds Increased Price Linkages between Commodities?* (working paper 2012); Le Pen and Sévi, *Futures Trading and the Excess Comovement of Commodity Prices* (working paper 2012); Creti, Joets, and Mignon, *On the Links Between Stock and Commodity Markets' Volatility, Energy Economics* (2010); Bichetti and Maystre, *The Synchronized and Long-lasting Structural Change on Commodity Markets: Evidence from High Frequency Data* (working paper 2012).

[1619] Boyd, Büyükşahin, and Haigh, *The Prevalence, Sources, and Effects of Herding* (working paper 2013); Hoff, *Herding Behavior in Asset Markets,* Journal of Financial Stability (2009). *See also* Froot, Scharfstein, and Stein, *Herd on the Street: Informational Inefficiencies in a Market with Short Term Speculation* (working paper 1990) (theoretical paper discussing herding); Weiner, *Do Birds of A Feather Flock Together? Speculator Herding in the Oil Market* (working paper 2006) (doing a herding analysis to conclude that there are subgroups within speculators that act in parallel, and this amplifies their effect on crude oil prices).

[1620] Hoff, *Herding Behavior in Asset Markets,* Journal of Financial Stability (2009); Mayer, *The Growing Interdependence Between Financial and Commodity Markets,* UN Conference on Trade and Development (discussion paper 2009) (Granger analysis).

[1621] *E.g.,* Brunetti and Büyükşahin, *Is Speculation Destabilizing?,* at 5 n.3 (working paper 2009) (''the moderate level of herding in futures markets [among hedge funds] serves to stabilize prices'').

[1622] Basu and Miffre, *Capturing the Risk Premium of Commodity Futures: The Role of Hedging Pressure,* Journal of Banking and Risk (2013).

[1623] *See* Aulerich, Irwin, and Garcia, *Bubbles, Food Prices, and Speculation: Evidence from the CFTC's Daily Large Trader Data Files,* at 3 n.4, NBER Conference on Economics of Food Price Volatility (2012) (studies testing for the existence of price bubbles in agricultural futures markets have led to ''mixed results''). *See also.*Belke, Bordon, and Volz, *Effects of Global Liquidity on Commodity and Food Prices,* German Institute for Economic Research (2013); Adämmer, Bohl and Stephan, *Speculative Bubbles in Agricultural Prices* (working paper 2011); Algieri, *A Roller Coaster Ride: an Empirical Investigation of the Main Drivers of Wheat Price* (working paper 2013); Babula and Rothenberg, *A Dynamic Monthly Model of U.S. Pork Product Markets: Testing for and Discerning the Role of Hedging on Pork-Related Food Costs,* Journal of Int'l Agricultural Trade and Development (2013); Windawi, *Speculation, Embedding, and Food Prices: A Cointegration Analysis* (working paper 2012).

[1624] Nobel laureates in economics cannot agree on whether bubbles exist or what the proper definition of a bubble is. Studies that focus on the causes of price formation avoid these definitional uncertainties. *See* Easterbrook, Frank, Monopoly, Manipulation, and the Regulation of Futures Markets, at S117, Journal of Business (1986) (it is

Continued

iii. Disadvantages

As applied to position limits, this approach has several drawbacks as well.

First and foremost, the analyses and conclusions that flow from these studies are only as good as the models themselves. Specifically, the price benchmark is based on the model, and an analysis of deviation from the benchmark is only as strong as the model itself. These models incorporate many simplifying assumptions. Market behavior and the real world in general, are much more complicated.

Moreover, these models do not function well when there is a supply shock or when demand falls precipitously. Another disadvantage is model construction using variables that are highly correlated with the price. If the correlation between price and a variable is too high, then using the variable in the model may permit the variable to function as a proxy for price. This will hobble the model's ability to detect price deviations.

A substantial disadvantage of this model is the inherent difficulty of modelling fundamentals of supply and demand in a market of any complexity. Or even, in a model, in anticipating or measuring the impact of large macroeconomic trends. For example, economists have a notoriously bad track record of predicting economic recessions. Thus it is difficult to conclude that a model with a few variables, designed without this hindsight, would be successful in predicting how crude oil prices would behave during the advent of an economic recession. With hindsight, economists know now that September 2008 was at the outset of a substantial global recession, or at least a point of dramatic decrease in the output of the world economy. And with hindsight, it is apparent that the recession dramatically reduced the demand for crude oil. But at the outset of a recession, a model designed without knowledge of the recession (or of its severity) might confuse a statistically significant deviation of actual crude oil prices for the fundamental price derived from the model.

In addition, while this statistical method replaces the loose language of ''bubbles'' with a statistically derived fundamental price, studies offering economic analysis of the fundamentals of price and demand do not eliminate all subjectivity in determining whether a non-fundament price has occurred. An economist will often obtain from these models a ''price band,'' a band for which prices falling within that range remain reflective of fundamental supply and demand. Prices outside the price band are non-fundamental prices. Determining the height of the band depends on what is viewed as a statistically significant deviation, by definition. But determining what a statistically significant deviation is requires the economist to make an assumption that can be quite consequential. The economist must set a level of price changes that his or her model will ignore as attributable merely to chance. Nothing in underlying statistics of the price data will provide the economist with this level. If the level is fixed so that the price band is relatively tall, less prices are likely to be labelled statistically significant deviation by the test.

iv. Analysis of Specific Papers Using Fundamental Models

Crude Oil Models

Even before 2007, there were suspicions about prices in the crude oil market. The Governor of the Federal Reserve Board said in 2004: ''The sharp increases and extreme volatility of oil prices have led observers to suggest that some part of the rise in prices reflects a speculative component arising from the activities of traders in the oil markets.'' [1625] Then the price of crude oil doubled from June 2007 to June 2008, and then rapidly declined in the second-half of 2008. Many economists thereafter published papers saying that the increase in demand up to June 2008 and/or the decrease in demand for September 2008 crude oil could not be explained by market fundamentals. Many attempted to infer from this fact that speculative trading was causing changes in crude oil prices or price volatility.

To understand these papers' strengths and weaknesses, it is important to appreciate a critical factor about crude oil market economics—storage.[1626] Data on storage is often used to study crude oil prices for speculative price influences.

Crude oil is storable, and so its price reflects, in particular, the demand for crude oil inventory. Speculators influence the spot price of crude oil by placing physical crude oil into storage when future prices are anticipated to be higher and out of storage when future prices are anticipated to be lower. Given this, some economists have studied crude oil storage to determine whether crude oil inventories could be contributing to the boom and bust in crude oil prices during the 2007–2008 time period. Specifically, using models of fundamental supply and demand, they study the elasticity of crude oil prices to determine whether the effect of speculators' trading on crude oil inventories could affect crude oil prices.

Several economists have examined above-ground oil inventories in the United States during this 2007–2008 timeframe and examined the interplay of crude oil inventories and prices. They concluded that the short-term elasticity of crude oil demand would have had to have been unusually low—quite inelastic—for inventory demand to fully explain the unusual crude oil prices in 2007–2008. (Price inelasticity of demand means that the price of crude oil is sensitive to changes in quantity demand: A small decrease in demand is likely to cause a large drop in price, for example, when the short-term elasticity of demand is inelastic, all else being equal.) From this, they conclude that speculative traders' effect on inventory demand was unlikely to be a complete explanation for the 2007–2008 crude oil price swings. That is, it would be unlikely for speculators to be able to (at least easily) cause substantial movements in crude oil prices by speculators' influence on the amount of crude oil stored in above-ground crude oil inventories.[1627]

Nonetheless, inventories may still explain part of the unusual price behavior of crude oil in 2007–2008. Even if the short-term elasticity of demand would have to have been very small in absolute value, speculation may have also affected below-ground inventories.[1628]

Many economists conclude that there was a substantial demand shock to crude oil during this time period, a

not necessarily market manipulation to exploit an advantageous position in the marketplace in anticipation of changes in supply and demand.'')

[1625] Ben S. Bernake, Oil and the Economy, Remarks by then Governor Bernake at the Distinguished Lecture Series, Darton College, Albany, Georgia (2004).

[1626] Brennan and Schwartz, *Arbitrage in Stock Index Futures* (Journal of Business 1990).

[1627] Byun, *Speculation in Commodity Futures Market, Inventories and the Price of Crude Oil* (working paper 2013); Hamilton, *Causes and Consequences of the Oil Shock of 2007–2008,* Brookings Paper on Economic Activity (2009); Kilian and Lee, *Quantifying the Speculative Component in the Real Price of Oil: The Role of Global Oil Inventories* (working paper 2013); Kilian and Murphy, *The Role of Inventories and Speculative Trading in the Global Market for Crude Oil,* Journal of Applied Econometrics (2010); Knittel and Pindyck, *The Simple Economics of Commodity Price Speculation* (working paper 2013).

[1628] Hamilton, *Causes and Consequences of the Oil Shock of 2007–2008,* Brookings Paper on Economic Activity (2009) (below-ground inventories should also be considered and are not included in the data) (concluding that speculative trading did affect both the speed and magnitude of the price decline in 2008).

demand arising from the onset of a global recession. As the deep recession of 2008 and 2009 began to set in, there was a decrease in demand for September 2008 crude oil in the crude oil futures market. It is unlikely that a demand shock associated with the recession was anticipated by the marketplace, including speculators, given the notorious difficulty of predicting recessions. Kilian and Murphy [1629] assert, if a global recession causes the demand shock, the economics of the crude oil market suggests that there is little policymakers can do to prevent this kind of price bubble from appearing in the crude oil market at the outset of the recession.[1630]

Several economists wrote papers suggesting that their results indicated that crude oil price changes during this time period reflected uneconomic or ''bubble-like'' behavior. Generally, these authors find that their models of supply and demand could not track well the run up in crude oil prices to around $145 in mid-2008 or the bust to close to $30 a barrel just a few weeks later, and they concluded that activity by speculators in these markets was or might be affecting the rapid crude oil price changes.[1631]

These studies do not, in total, lead to consensus. There are distinctive differences and disagreement in the papers on the existence of excessive speculation in the crude oil market during 2007–2009. Even within the Federal Reserve system, there is disagreement, for instance, Plante and Yücel, in *Did Speculation Drive Oil Prices? Futures Market Points to Fundamentals,*[1632] and Juvenal and Petrella, in *Speculation in the Oil Market.*[1633]

The methodology of fundamentals of supply and demand does not zero in precisely on causation and leaves room for interpretation of why a price does not follow modelled supply and demand behavior. Labelling prices ''bubbles'' caused by speculation simply because one does not understand or cannot otherwise account for price movements is problematic. One explanation for the failure of these models to track such fast-moving prices that is speculative activity is at work. But there are other explanations. On some level, there is a tautological error in labelling price changes as ''bubble-like'' simply because economists could not, as of a certain time and with certain model, otherwise explain or predict price movements. These models are trying to explain very complex phenomena and make difficult choices on how to use imperfect data.

Some models performed better at modelling the real-world crude oil prices, using models of fundamental supply and demand, by selecting one of the stronger proxies for crude oil, such as the Dry Baltic Index or macroeconomic variables such as global gross domestic product as explanatory variables.[1634]

One of the best studies in this area is Hamilton, *Causes and Consequences of the Oil Shock of 2007–2008.*[1635] He concludes that fundamentals of supply and demand are responsible for most of the run-up in prices, while speculative trading may have increased both the speed and absolute magnitude of the mid-2008 decline in prices. As to the first point, he concludes that while oil prices may have been ''too high'' in July 2008, ''low price elasticity of demand, and the failure of physical production to increase'' are more likely the predominant causes than ''speculation per se.'' [1636] He acknowledges, however, that the speed and magnitude of the price decline in mid-2008 may have been induced, in part, by speculative trading.

Given this mixed result, both proponents and opponents of position limits cite various aspects of this Hamilton study. His study follows the data closely; his model discusses key issues such as inventory. He does not leap to strained interpretations based on theoretical model assumptions. When his model does not provide a full explanation for price behavior based on supply and demand, he does not simply jump to the conclusion that speculation is at work. Instead, he offers measured

[1629] Kilian and Murphy, The Role of Inventories and Speculative Trading in the Global Market for Crude Oil, Journal of Applied Econometrics (2010).

[1630] *See id.* at 6 & n. 8 (economic theory suggests a link between cyclical fluctuations in global real activity and the real price of oil).

[1631] *E.g.,* Cifarelli and Paladino, Oil Price Dynamics and Speculation: A Multivariate Financial Approach, at p.1, Energy Economics (2010) (''Despite the difficulties, we identify a significant role played by speculation in the oil market, which is consistent with the observed large daily upward and downward shifts in prices—a clear evidence that it is not a fundamental-driven market''); Einloth, Speculation and Recent Volatility in the Price of Oil (working paper 2009) (using convenience yields to conclude that speculation did not play a major role in rise of crude oil to $100 a barrel in March of 2008, did play a role in its subsequent rise to $140 a barrel, and did not play a role in subsequent decline); Hamilton, Causes and Consequences of the Oil Shock of 2007–2008, Brookings Paper on Economic Activity (2009) (speculative trading increased the speed and magnitude of mid-2008 price collapse). Papers using this methodology reach a broad range of conclusions. *See also* Eckaus, The Oil Price Really is a Speculative Bubble (working paper 2008) (reject the hedging pressure hypothesis that inventory positions are an important determinant of risk premiums, and concludes that oil prices are speculative because he cannot perceive a reason for the prices based on supply and demand); Morana, Oil Price Dynamics, Macro-finance Interactions and the Role of Financial Speculation, at 206–226, Journal of Banking & Finance, Vol. 37, Issue 1 (Jan. 2013) (concluding that there is excessive speculation in the crude oil market that did lead to a substantial price impact in 2007–2008); Sornette, Woodard and Zhou, The 2006–2008 Oil Bubble and Beyond: Evidence of Speculation, and Prediction, Physica A. (2009) (find evidence of a bubble, but only based upon an undocumented model largely presented by graphs); Stevans and Sessions, Speculation, Futures Prices, and the U.S. Real Price of Crude Oil, American Journal of Social and Management Science (2010) (contending that there is ''hoarding'' in the crude oil market and that elimination of the longer-term futures contracts would curb excessive speculation); Weiner, Speculation in International Crises: Report from the Gulf, Journal of Int'l Business Studies (2005) (a combination of political and market events, not speculation, was behind the price volatility in 1990–1991); Breitenfellner, Crespo, and Keppel, Determinants of Crude Oil Prices: Supply, Demand, Cartel, or Speculation?, at 134, Monetary Policy and the Economy (2009) (concluding ''it is conceivable'' that interaction between crude oil production and financial markets exacerbated pressure on crude oil prices, but finding no proof of this).

[1632] Plante and Yücel, Did Speculation Drive Oil Prices? Futures Market Points to Fundamentals (working paper Federal Reserve of Dallas 2011) (crude oil data for the 2007–2009 time period ''are consistent with how a well-functioning futures market would behave,'' and if speculation had been to blame, there would have been ''very large positive spreads . . . followed by significant increases in inventory'').

[1633] Juvenal and Petrella, Speculation in the Oil Market (working paper of Federal Reserve Bank of St. Louis 2012) (concluding that speculation played a ''significant role'' in both the price increases in 2008 and the subsequent collapse, but they did not carefully model ''excess speculation.'' Instead, they interpreted the second principle component as being ''excess speculation'' even though the second component may be assigned many other interpretations or even be deemed uninterpretable.).

[1634] *E.g.,* Kilian and Murphy, The Role of Inventories and Speculative Trading in the Global Market for Crude Oil, Journal of Applied Econometrics (2010). In the construction of his study, Kilian used a shipping index, the Dry Baltic Index. In shipping, a predominant factor in the cost of shipping is the cost of crude oil. By using the Dry Baltic Index to attempt to compose a model to explain crude oil prices, the economist chose a variable which would naturally be highly correlated to crude oil prices. However, by using a proxy, the effectiveness of the model is lessened. It is unclear whether the results are attributable to fundamentals driving crude oil prices or crude oil prices driving the Dry Baltic Index. *See also* Morana, Oil Price Dynamics, Macro-finance Interactions and the Role of Financial Speculation, pp. 206–226, Journal of Banking & Finance, Vol. 37, Issue 1 (Jan. 2013) (careful, large-scale modeling of the oil market macro-finance interface, finding the existence of ''excess speculation'' in these markets using Workings T and other tests, and concluding that financial factors may have up to a 30 percent contribution to oil price fluctuations). *Id.* at p.220 (using Working's T and model to conclude that there is a significant liquidity effect associated with non-fundamental financial shocks in the oil market, leading to a higher real oil price without affecting inventories); *id.* at 223–224 (macro-finance factors played a larger role than ''financial factors'' in the 2007–2009 crude oil ''price shock,'' but ''excessive speculation'' did have a price impact).

[1635] Hamilton, Causes and Consequences of the Oil Shock of 2007–2008, Brookings Paper on Economic Activity (2009).

[1636] *See id.* at 17–23.

judgments on the possibility that speculation may have affected the precipitous mid-2008 crude oil price decline and presents statistical evidence that this *may have* occurred.

Other Studies Based on Supply and Demand Models

A discussion of crude oil prices during the 2007–2008 timeframe is illustrative of other commodities during this time period. For example, there is considerable comovement between the real price of crude oil and the real price of other industrial commodities during times of major fluctuation in global real activity (such as global recessions).[1637] All commodities during this time period were buffeted by macroeconomic factors, including a global recession, and a deep one at that during 2008 and 2009.

Outside of the crude oil context, there are some noteworthy studies of fundamental supply and demand that bear on the position limits rulemaking.

Allen, Litov, and Mei, in *Large Investors, Price Manipulation, and Limits to Arbitrage: An Anatomy of Market Corners,*[1638] examine historical corners and squeezes in security and commodity markets and conclude that a corner or squeeze may induce arbitragers to exit the market, since arbitragers will only take short positions when the prospect of profits is high enough. Two papers, Gorton, Hayashi, Rouwenhorst, *The Fundamentals of Commodity Futures Returns,*[1639] and Ederington, Dewally, and Fernando, *Determinants of Trader Profits in Futures Markets,*[1640] offer empirical support for the hedging pressure hypothesis: That the returns on long futures positions vary inversely with inventory and price volatility.[1641] Haigh, Hranaiova, and Overdahl, in *Hedge Funds, Volatility, and Liquidity Provisions in the Energy Futures Markets,*[1642] suggest that hedge funds supply liquidity and that there is little linkage between price volatility and hedge fund position change. They claim that hedge fund participation in futures markets, at least as of 2007, was not injecting unwarranted volatility into futures prices.[1643]

Other papers on the fundamentals of supply and demand do not bear directly on position limits. Some discuss matters far afield from the impact of positions on price or other matters bearing on position limits.[1644] Others rest on unreliable model assumptions.[1645]

[1637] Kilian and Murphy, The Role of Inventories and Speculative Trading in the Global Market for Crude Oil, at p.7 n. 9, Journal of Applied Econometrics (2010).

[1638] Allen, Litov, and Mei, Large Investors, Price Manipulation, and Limits to Arbitrage: An Anatomy of Market Corners, Review of Finance (2006).

[1639] Gorton, Hayashi, Rouwenhorst, The Fundamentals of Commodity Futures Returns, Review of Finance (2013).

[1640] Ederington, Dewally, and Fernando, Determinants of Trader Profits in Futures Markets (working paper 2013).

[1641] All else being equal, the more inventory available for delivery the less costly it is for shorts to hedge their exposure. Similarly, the more volatile the commodity prices are, the more price risk is being accepted by the longs (all else being equal). This means that in volatile markets hedgers that are short will pay higher risk premia to hedge.

[1642] Haigh, Hranaiova, and Overdahl, Hedge Funds, Volatility, and Liquidity Provisions in the Energy Futures Markets, Journal of Alternative Investments (2007).

[1643] *See also* Harrison and Kreps, Speculative Investor Behavior in a Stock Market With Heterogeneous Expectations, Quarterly Journal of Economics (1978) (differences in subjective beliefs induce trading and speculation); Manera, Nicolini and Vignati, Futures Price Volatility in Commodities Markets: The Role of Short-Term vs Long-Term Speculation (working paper 2013) (short-term speculation, as estimated by daily volume divided by open interest, increases volatility while long term speculation, using a Working's T analysis, decreases it); Trostle, Global Agricultural Supply and Demand: Factors Contributing to the Recent Increase in Food Commodity Prices, USDA Economic Research Service (2008) (surveying supply and demand fundamentals explain a lot of the futures prices and price volatility: Slow growth in production relative to demand for biofuels, declining US dollar, rising oil prices, bad weather 2006 to 2007, growing holdings by foreign countries, and increased cost of production for agriculture in general).

[1644] Chan, Trade Size, Order Imbalance, and Volatility-Volume Relation, Journal of Financial Economics (2000) (studying the equity market to determine the role that trade size has on volatility for equities); Chordia, Subrahmanyam and Roll, Order imbalance, Liquidity, and Market Returns, Journal of Financial Economics (2002) (show that order imbalances in either direction for equity markets affect daily returns after controlling for aggregate volume and liquidity); Doroudian and Vercammen, First and Second Order Impacts of Speculation and Commodity Price Volatility (working paper 2012) (claiming a ''second order'' price distortion caused by institutional investors); Frankel and Rose, Determinants of Agricultural and Mineral Commodity Prices (working paper 2010) (two macroeconomic fundamentals—global output and inflation—have positive effects on real commodities, but microeconomic variables have greatest overall effects, including volatility, inventories, and spot-forward spread); Girardi, Do Financial Investors Affect Commodity Prices? (working paper 2011) (during the late 2000s there was a positive, statistically significant and substantial correlation between hard red winter wheat price and the U.S. equity market, as well as a substantial correlation between hard red winter wheat prices and crude oil prices); Hong and Yogo, Digging into Commodities (working paper 2009) (investors use commodities to hedge market fluctuations, as evidenced by yield spread analysis); Kyle and Wang, Speculation Duopoly with Agreement to Disagree: Can Overconfidence Survive the Market Test?, Journal of Finance (1997) (theoretical model explaining how overconfidence by fund managers can lead to a persistence in market prices); Plato and Hoffman, Measuring the Influence of Commodity Fund Trading on Soybean Price Discovery (working paper 2007) (''finding that the price discovery performance of the soybean futures market has improved along with the increased commodity fund trading''); Westcott and Hoffman, Price Determination for Corn and Wheat: The Role of Market Factors and Government Programs (working paper 1999) (analysis of supply and demand fundamentals for wheat and corn that does not include position data); and Wright, International Grain Reserves and Other Instruments to Address Volatility in Grain Markets, World Bank Research Observer (2012) (about price limits, not position limits).

[1645] Bos and van der Molen, A Bitter Brew? How Index Fund Speculation Can Drive Up Commodity Prices, Journal of Agricultural and Applied Economics (2010) (most of the changes in spot prices can be attributed to shifts in demand and supply, and failure to account properly for these inputs in the coffee price generation process may lead to serious overestimation of the effects of speculation; nevertheless, asserting without detailed analysis that speculation is an important part of the coffee price generation process), Gupta and Kamzemi, Factor Exposures and Hedge Fund Operational Risk: The Case of Amaranth (working paper 2009) (trying to explain the behavior of Amaranth on the mistaken notion that a hedge fund should be diversified); Henderson, Pearson and Wang, New Evidence on the Financialization of Commodity Markets (working paper 2012) (analysis founded on questionable assumption that commodity link note investors are uninformed investors); Van der Molen, Speculators Invading the Commodity Markets (working paper 2009) (data handling problems: Dataset which covers twenty years, while the variable index speculators is only available for two to three years, and assumes that net position is in indication of index speculators).

d. Switching Regressions

i. Switching Regression Analysis Described

In a switching regression analysis, an economist poses the existence of a model with more than one state. In the particular context of position limits, there are typically two states: (1) A normal state—where prices are viewed as what they theoretically should be following market fundamentals and (2) a second state—often described as a ''bubble'' state in these papers. Using price data, authors of these studies calculate the probability of a transition between these two states. The point of transition between the two states under this methodology is called a structural ''breakpoint.'' Examination of these breakpoints permits the researcher to date and time the existence of a second state, such as a bubble state.

These authors sometimes find empirical support in the data for the existence of a second state by calculating the probability of breakpoints. When the probability is high enough, the research will say that there is evidence for a second state.

ii. Advantages

A variant of this method was first published in 1973. It is fairly well-credentialed within academia. If there are two states of the world, it makes sense that distinct states would have different economic models. Because switching regressions uses at least a two-state regression, this method satisfies the economist's view that different states would be better described using different models. A one-size-fits-all model, applied to varying economic states, could potentially be compromised in order to accommodate disparate states.

This model is flexible, allowing for many different specifications (of model design) as explanatory variables of speculative positions and futures prices.

When using this method, the economic researcher permits the data itself to choose the structural breakpoints. This differs from some other statistical methods, where the economic researcher may choose exogenously, based on interpretation of the data or historical knowledge, where and when a transition to a supposed bubble state occurs. The model's selection of the breakpoint permits data to be tested against known historical events and thus lend a measure of credence to the model's choices for structural breaks.

The model also permits close study of particular time periods. An economist may well be aware of historical events that were market-transition events such as ''bubbles,'' and this method permits the economist to zero-in on that time period and to investigate potential causes and/or confounding events associated with a suspected market transition.[1646]

iii. Disadvantages

This method has a significant disadvantage that is highlighted in the position limit context. This statistical technique tests for a second state. There could, however, be reasons for a non-normal state other than a ''bubble'' state. This method leaves quite a bit to economic interpretation of the model, not raw data analysis, to reach their inference that the second state is a ''bubble'' state.

While the existence of a second state may indicate a ''bubble'' state and may indicate a problem with excessive speculation, this statistical method cannot definitively prove these inferences, even if position data were used in the analysis. The probability of the existence of second state in these studies in only circumstantial evidence of (1) a ''bubble'' state and (2) a ''bubble'' state caused by excessive speculation.

Consider an example of why data alone cannot explain why a deviation from a normal market state is a bubble state: The case of feeder cattle. If there is a drought and feed becomes scarce and expensive, the cattlemen may sell off part of their herd. Prices of feeder cattle may then drop in the short term as well, because cattleman may sell young calves, too. But subsequently, because so many cattle have been slaughtered, there is a shortage of feeder cattle the next season and the prices of feeder cattle rise. So in this case, there is theoretical and empirical support for two states, but they correspond to non-drought and drought states and not normal and ''bubble'' state. Switching regression analysis if applied to feeder cattle prices during a time period encompassing both drought and non-drought state would not establish the existence of what we could typically view as a ''bubble'' in the post-drought price rise.[1647] In any event, none of this price phenomenon can be viewed as a problem of ''excessive speculation.'' One could still use the ill-defined word ''bubble'' to describe the second state, but it would be a dearth of rainfall, not excessive speculation, which created this second state.

The theoretical level of the analysis, and in particular the lack of firm empirical data linking non-normal states to speculative ''bubble'' markets, are weaknesses of this statistical method. The studies following this method do not provide categorical proof of the existence of speculative ''bubble'' markets and they do not provide statistical evidence of whether positions limits would be effective in ameliorating ''bubble'' markets.[1648]

iv. Analysis of Studies Reviewed That Used Switching Regression

Five studies used a standard form of switching regressions analysis.[1649]

[1646] This method is particularly good at ''accommodating'' abrupt shifts in market data. Some statistic methods, such as those based on linear regression, may have difficulty with volatile data or data discontinuity. This method is also particularly well-suited for studying policy changes. For example, if the Federal Reserve makes a policy change that is expected to have a long-term, but not necessarily an immediate, impact, this method will permit an economist to infer, based on the model, the duration of the lag before the policy change begins to affect the markets.

[1647] This example is taken from an academic paper not within the administrative record that found non-fundamental (or ''bubble'') prices in crude oil and feeder cattle markets. Brooks et al, Boom and Busts in Commodity Markets: Bubbles or Fundamentals? (working paper 2014).

[1648] These models are difficult to design well in this context for several other reasons. The economist is making an informed, probabilistic inference that a transition has occurred. This inference is more than a seat-of-the-pants determination, but it is less than a mathematical certainty. The result of this statistical method is also highly dependent upon what set of data the econometrician selects for analysis. An economic model founded on this method should be given more credence when it is applied to more than one dataset and the results are replicated with different data. Selection of controlling variables that would account for position data is a difficult task with this statistical model. The data-driven nature of the model does not help in selection of proper controlling and explanatory variables. Ingenuity is required to design explanatory variables that would account well for position data.

[1649] These are: Cifarelli and Paladino, Commodity Futures Returns: A non-linear Markov Regime Switching Model of Hedging and Speculative Pressures (working paper 2010) (concluding that speculation, not supply and demand factors, drive some daily price swings in certain energy futures); Chevallier, Price Relationships in Crude oil Futures: New Evidence from CFTC Disaggregated Data, Environmental Economics and Policy Studies (2012) (the influence of financial investors through the S&P GSCI Energy Spot may have contributed to price changes in the crude oil market) (discussed in ensuing text); Hache and Lantz, Speculative Trading & Oil Price Dynamic: A Study of the WTI Market, Energy Economics, Vol. 36, 340 (March 2013) (cannot reject hypothesis that variations in the positions of non-commercial players may have played a ''destabilising role in petroleum markets'' and ''speculative trading can be considered an important factor during market instability and 'oil bubbling' process''); Lammerding, Stephan, Trede, and Wifling, Speculative Bubbles in Recent Oil Price Dynamics: Evidence from a Bayesian Markov Switching State-Space Approach, Energy Economics Vol. 36 (2013) (claims to find robust evidence of ''bubbles'' in oil prices associated with speculation); and Sigl-Grüb and Schiereck,

Continued

Three studies used a related methodologies, multi-state regressions or conditional correlations.[1650]

Most of these studies are not helpful because they do not use position data or because they have technical issues.[1651] It is difficult to perform these types of studies well. A study finding the existence of transitions between states can be unconvincing if it does not have solid theoretical and economic justifications for the data selected and the model's design. Many of the disadvantages of this methodology, discussed above, find expression in these papers.

However, there is one switching regression study worthy of further discussion in our view. It is well-executed and employs position data: Chevallier, *Price Relationships in Crude oil Futures: New Evidence from CFTC Disaggregated Data.*[1652] Of course, it inherits all the difficulties of speculative position data, such as the difficulty separating hedgers from speculators. Yet Chevalier's effort does persuasively suggest the existence of two states in price structure during 2008 crude oil market price swings. His paper suggests that with highly inelastic supply and demand, the influence of financial investors through the S&P GSCI Energy Spot may have contributed to price changes in the crude oil market.

Using switching regressions, Chevallier attempts to reconcile two strands of economic literature: Papers that posit the predominance of supply and demand fundamentals and other papers that investigate speculative trading. Chevallier employs macroeconomic variables, proxies for supply and demand fundamentals, and speculative positions (net open position of speculators) in his model specifications. Using switching regression analysis, he concludes that one cannot eliminate the possibility of speculation (a reason why the physical commodity may move into and out of storage) as one of the main reasons behind the 2008 oil price swings.

This is an important result. Other economic studies using models of supply and demand purport to explain the 2008 price swings in crude oil without incorporating speculation into demand. Chevallier's paper suggests that speculation cannot be ruled out as a cause. Specifically, using net speculative positions as one of his variables in his test, he found that this variable was statistically significant on crude oil futures natural logarithm of price returns during the 2008 time period.[1653]

This result posits that speculation may have played some role during the 2008 crude oil futures price swings. It suggests that studies that look only to supply and demand without incorporating speculative demand to explain the crude oil market in 2008 may be overlooking an important factor. The switching regression methodology in this context functions as a cross-check to determine whether models of fundamental supply and demand can, in fact, account for all the price swings in crude oil during this time. In at least this particular commodity market and timeframe, Chevallier's finding that net speculative positions are correlated with crude oil future prices suggests a price effect from net speculative positions.

e. Eigenvalue Stability

i. Description

Some economists have run regressions on price and time-lagged values of price. They estimate the time-lagged regression over short time internals. They do this to detect, through examination of specific terms in their lagged price model, unusual price changes. In technical terms, they use a difference equation for lagged price with different estimated values (*i.e.,* coefficients) for different time-lagged price variables. They then solve for the roots of that characteristic equation and look for the eigenvalues (latent values) with absolute value greater than one. They conclude that eigenvalue indicates that the price of the commodity is in an ''exploding'' state or a ''bubble.'' [1654]

ii. Advantages and Disadvantages

This method can be applied after-the-fact to historical data to try to ascertain whether past price changes constituted a ''bubble.'' Or it can be applied to real-time data to predict whether a current state of affairs is a ''bubble.'' For these reasons, some economists perceive, as an advantage of this method, the ability through statistical means to date and time ''bubbles'' in prices.

On the other hand, this method is based on a model and the results of any analysis are only as strong as the model. The model is limited to price data and a constant. Models using this technique do not permit the study authors to include other explanatory variables. This is a disadvantage because it is likely that there are variables of interest other than lagged prices when considering whether price instability exists. For example, someone interested in position limits would want to include an explanatory variable such as speculative positions in the regressions, but this technique does not permit this.

Further, the model allows for wide discretion in the number of lagged prices used. The studies' authors often look at ''goodness of fit'' results to determine how many lags to select, seeking to set the model based upon the data. This step may make the model uniquely tailored to a particular dataset but not easily applicable to another. Put another way, selecting an important model feature based on testing of the data runs the risk of a selection that is not based on any theoretical or economic fact, but instead on ad hoc assumptions made by the modelers and any idiosyncrasies of the dataset.[1655]

iii. Analysis

Economists using this methodology attempt to find the existence of price ''bubbles'' using eigenvalue stability methods. Three such papers were

Speculation and Nonlinear Price Dynamics in Commodity Futures Markets, Investment Management and Financial Innovations, Vol. 77, pp. 59–73 (2010) (''short-run autoregressive behavior'' of commodity markets is driven not only by fundamentals but also by trading of speculators).

[1650] These are: Fan and Xu, What Has Driven Oil Prices Since 2000? A Structural Change Perspective, Energy Economics (2011) (multi-state); Baldi and Peri, Price Discovery in Agricultural Commodities: The Shifting Relationship Between Spot and Futures Prices (working paper 2011) (multi-state); Silvernnoinen and Thorp, Financialization, Crisis and Commodity Correlation Dynamics, Journal of Int'l Financial Markets, Institutions, and Money (2013) (conditional correlations). All three of these papers are of mixed methodology, applying switching regression analysis to relationships between prices that are viewed by the papers' authors as cointegrated.

[1651] For example, the study by Sigl-Grüb and Schiereck employs a smooth transition (as opposed to an abrupt change) between states. Unfortunately, the study's model does not have a high goodness-of-fit values (all adjusted-$R^2$ are below 0.05 and most are below 0.01), nor fundamental economic explanatory variables (only lagged prices and speculative positions in the transition component between states). These are shortcomings. In particular, the latter omission may overstate the importance of speculative positions.

[1652] Chevallier, *Price Relationships in Crude oil Futures: New Evidence from CFTC Disaggregated Data,* Environmental Economics and Policy Studies (2012).

[1653] Specifically, Chevallier found that in the first state, the coefficient of the logarithmic returns of net speculative positions is positive and significant (1 percent level). In the second state, this coefficient is negative and mildly significant (10 percent level). Chevallier's results show statistically significant relationships between the volume of speculative positions in particular and logarithmic price returns.

[1654] *See, e.g.,* Goyal and Tripathi, Regulation and Price Discovery: Oil Spot and Futures Markets at 15–16 (working paper 2012) (describing methodology in more detail).

[1655] Even if there were not such problems, the methodology has an insurmountable theoretical difficulty. The use of the ''unit root'' test, as a part of this eigenvalue methodology, is an inherently suspect way of identifying explosive price behavior. That is because the unit root tests rely upon a small a set of observations to approximate long-term price behavior.

submitted.[1656] All the authors find ''evidence'' of various ''bubbles.'' However, in none of these studies is there reasonable empirical evidence to support the inferential leap between instability, ''bubbles,'' and excess speculation. In particular, for all of these studies, there is no link made in the data between price instability and positions. These studies do not use position data. The problem inheres in the method, which, while purporting to detect the existence of ''bubbles,'' does not permit the research to link supposed bubble to speculative positions.

In modern markets, prices can change rapidly for many reasons. The ''explosion'' of a price over a short time interval does not necessarily reflect uneconomic behavior or a price ''bubble.'' It could simply represent a ''shock.'' That shock need not come from speculative activity. The price path may not be smooth. For this reason, these models are conceptually flawed when applied to commodity prices and commodity futures prices.

For example, in Gilbert, *Speculative Influences on Commodity Futures Prices,*[1657] Gilbert uses a variant of this methodology in an early section of his paper to find ''clear evidence'' of ''bubble periods'' for copper and soybeans lasting days and weeks.[1658] He finds unexplained price increases in crude oil for periods of time that are ''insufficient to qualify as bubbles.'' [1659] Using just price data, and not positions, Gilbert's attribution of lingering price spikes cannot be attributed to speculative positions.[1660]

There is a subtler disadvantage that inheres in the inference between the identification of price growth without bound and the existence of a bubble. To examine intervals where a price series is appearing to grow without bound and to infer that that implies a bubble is problematic. A time series for price of an asset is unlikely to tend to infinity because, eventually, this would likely lead to infeasible prices (generally, in the absence of hyperinflation). We do not expect the real price of an asset, which is the price is adjusted for inflation, to grow without bound.

2. Theoretical Models

Some economic papers cited in this rulemaking perform little or no empirical analysis and instead, present a general theoretical model that may bear, directly or indirectly, on the effect of excessive speculation in the commodity marketplace. Within the 26 theoretical model papers in the administrative record, there is a subset of papers which may be viewed as generally supportive or disapproving of position limits. Because these papers do not include empirical analysis, they contain many untested assumptions and conclusory statements. In the specific context of academic analysis of position limits (as opposed to policy formulation) theories are useful but must be tested empirically.

Theoretical Papers Directly or Indirectly Support Position Limits

Two studies presented theoretical models establishing the risk of price manipulation in the derivatives markets, including cash-settled contracts, suggesting that position limits might be particularly helpful in cash-settled contracts.[1661] A few studies presented theoretical reasons why financial investors might increase or ''destabilize'' commodity futures prices [1662] or the spot price.[1663]

Theoretical Studies Indirectly Criticizing at Least Some Position Limits

On the other hand, there were theoretical papers that reached conclusions which could be helpful to position limit skeptics, such as the power of the marketplace to ''self-discipline'' would-be excessive speculators.[1664] Some papers offer theoretical grounds for the concern that more restrictive or ''extreme'' position limits might increase price volatility.[1665]

Even these papers are not firm in their opposition. In *The Self-Regulation of Commodity Exchanges: The Case of Market Manipulation,* Journal of Law and Economics (1995),[1666] Craig Pirrong (an economic expert for ISDA/SIFMA in the position limits rulemaking) argues that there ''is no strong theoretical or empirical reason to believe that self-regulating exchanges effectively deter corners.'' [1667] He simply disagrees that other forms of regulation such as position limits ''could do better.'' [1668] Pirrong does not discount the harm of price manipulation. Pirrong's *Manipulation of the Commodity Futures Market Delivery Process,*[1669] documents these harms.[1670]

Other Theoretical Papers

A set of papers suggest that there can be excessive speculation in oil without

[1656] These are: Phillips and Yu, Dating the Timeline of Financial Bubbles During the Subprime Crisis, Quantitative Economics (2011); Czudaj and Beckman, Spot and Futures Commodity Markets and the Unbiasedness Hypothesis—Evidence from a Novel Panel Unit Root Test, Economic Bulletin (2013); Gutierrez, Speculative Bubbles in Agricultural Commodity Markets, European Review of Agricultural Economics (2012) (Monte Carlo variant of eigenvalue stability approach).

[1657] Gilbert, Speculative Influences on Commodity Futures Prices, 2006–2008, UN Conference on Trade and Development (2010).

[1658] *Id.* at 9 at ¶ iii.

[1659] *Id.* at ¶ ii.

[1660] This is perhaps why he proceeds to a Granger-based analysis using position data in the second half of his paper.

[1661] Kumar and Seppi, Futures Manipulation with ''Cash Settlement'', Journal of Finance (1992) (while, without physical delivery, corners and squeezes are infeasible, cash-settled contracts are still susceptible to cash-to-futures price manipulation, and this price manipulation transfers liquidity from futures to cash markets); Dutt and Harris, Position Limits for Cash-Settled Derivative Contracts, Journal of Futures Markets (2005) (arguing that cash settled contracts appear to be particularly susceptible to manipulation, but appearing to conflate SEC options with CFTC-regulated commodity contracts).

[1662] Lombardi and van Robays, Do Financial Investors Destabilize the Oil Price? (working paper, European Central Bank, 2011) (giving theoretical grounds for the ability of financial investors in futures to destabilize oil prices, but only in the short run); Vansteenkiste, What is Driving Oil Price Futures? Fundamentals Versus Speculation (working paper, European Central Bank, 2011); Liu, Financial-Demand Based Commodity Pricing: A Theoretical Model for Financialization of Commodities (working paper 2011).

[1663] Schulmeister, Torero, and von Braun, Trading Practices and Price Dynamics in Commodity Markets (working paper 2009) (finding that price movements in crude oil and wheat are lengthened and strengthened by ''speculation'' in respective futures prices).

[1664] Pirrong, Manipulation of the Commodity Futures Market Delivery Process, Journal of Business (1993); Pirrong, The Self-Regulation of Commodity Exchanges: The Case of Market Manipulation, Journal of Law and Economics (1995); Ebrahim and ap Gwilym, Can Position Limits Restrain Rogue Traders?, at 832 Journal of Banking & Finance (2013) (''Our results illustrate that excess speculation, with or without the intent to manipulate the futures markets, is not worthwhile for the speculator'' and concluding that position limits are ''counterproductive'' because excessive speculation enriches other market players at the expense of the speculator).

[1665] Pliska and Shalen, The Effects of Regulation on Trading Activity and Return Volatility in Futures Markets, at 148, Journal of Futures Markets (2006) (''[W]ell-meaning regulatory policies can be counterproductive by reducing the liquidity which is characteristic of futures markets,'' including policies such as ''extreme margins and position limits''); Lee, Cheng and Koh, An Analysis of Extreme Price Shocks and Illiquidity Among Systematic Trend Followers (working paper 2010) (using an agent-based model and assuming trend-followers in the market, finds no reason to believe position limits will help as opposed to leading to erratic price behavior).

[1666] Pirrong, The Self-Regulation of Commodity Exchanges: The Case of Market Manipulation, Journal of Law and Economics (1995).

[1667] *Id.* at 143.

[1668] *Id.* (asserting that position limits are ''excessively costly'' and concluding that self-regulation, along with after-the-fact civil and criminal penalties for manipulation, may be more efficient, but this assertion is unaccompanied by quantitative analysis or a detailed qualitative cost-benefit analysis).

[1669] Pirrong's Manipulation of the Commodity Futures Market Delivery Process, Journal of Business (1993).

[1670] *Id.* at 363 (futures market manipulations ''distorts prices and creates deadweight losses;'' ''causes shorts to utilize real resources to make excessive deliveries;'' and ''distorts consumption'').

a significant increase in crude oil inventories.[1671] The remaining theoretical papers in the administrative record focus on useful economic background on price manipulation;[1672] comovement effects in the equity or options markets,[1673] high-frequency trading,[1674] or other matters of marginal relevance.[1675]

3. Surveys and Opinions

The remaining 73 papers are survey pieces. Some of these papers provide useful background material.[1676] But on the whole, these survey pieces offer opinion unsupported by rigorous empirical analysis. These papers, if they presented statistics at all, presented descriptive statistics. An inherent difficulty with this approach is that the facts that the author presents to support the author's theory may be incomplete and not fully representative of economic reality.

While they may be useful for developing hypotheses, they often exhibit policy bias and are not neutral, reliable bases for judgments in the academic context (again, as opposed to the judgments of policymakers).[1677]

We have reviewed all 73 papers in this category and discuss below only those few that add marginal value to the empirical analyses discussed above.

a. Frenk and Turbeville (Better Markets)

Frenk and Turbeville, in *Commodity Index Traders and the Boom/Bust Cycle in Commodities Prices,*[1678] present a survey of economic literature that incorporates some empirical testing for the price impact of index fund ''rolling'' of commodity index fund positions. Rolling refers to the time when commodity index funds, such as those tracking a popular commodity index such as the Standard & Poor's Goldman Sachs Commodity Index (GSCI), must roll forward their expiring futures contracts to maintain their (typically long) positions.[1679] Frenk and Turbeville argue that the index fund roll ''systematically distorts forward commodities futures price curves toward a contango[1680] state, which is likely to contribute to speculative 'boom/bust' cycles. . . .''[1681]

This set of inferences is problematic for several reasons. First, it depends on the current existence of a price impact from rolling. Yet the roll price impact is a market phenomenon that may no longer be as substantial as it once was. The market now has general knowledge of the influx of commodity index traders and their established rolling behavior. Moreover, many ETFs announce in their prospectus how they will trade, and most large exchange-traded funds now ''sunshine'' their rolls: To announce to the market in advance when and how they will roll.[1682] These trends have lessened the price impact of the rolls.

Moreover, the Frenk and Turbeville article ascribes the contango state of commodity futures prices to the price impact of roll without empirical analysis to support a causal link. There has historically been an alternation between contango and backwardation in the crude oil commodity market: This phenomenon has been attributed to changes in short-term supply or demand, increased market participation on the long side to earn the risk premium associated with going long, and other reasons, but not the technical aspects of commodity index rolls.[1683] Frenk and Turbeville's article is unpersuasive in ascribing large boom/bust cycles in price to waning and temporary price impacts of rolls.

Several other survey papers posit the existence of a speculative bubble in price due to speculation along the lines of the Frenk and Tuberville article. But these studies also do not present an empirical analysis to support this conclusion.[1684]

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[1671] Avriel and Reisman, *Optimal Option Portfolios in Markets with Position Limits and Margin Requirements,* Journal of Risk (2000) (a theoretical model suggesting that speculation may push crude oil prices above the price level is justified by physical-market fundamentals without necessarily resulting in a significant increase in oil inventories); Pierru and Babusiaux, *Speculation without Oil Stockpiling as a Signature: A Dynamic Perspective* (working paper 2010); Routledge, Seppi, and Spatt, *Equilibrium Forward Curves for Commodities,* Journal of Finance (2000) (important work on the theory of storage). *See* Parsons, *Black Gold & Fool's Gold: Speculation in the Oil Futures Market* at 82, 106–107 (Economia 2009) (not a theoretical model paper, but a survey piece, that indicates that if oil prices were driven above the level determined by fundamental factors of supply and demand by forces such as speculation, storage would not necessarily increase; an argument that this would occur ''overlooks how paper oil markets have been transformed'' and ''successful innovations in the financial industry made it possible for paper oil to be a financial asset in a very complete way'').

[1672] Kyle and Viswanathan, How to Define Illegal Price Manipulation, American Economic Review (2008); Westerhoff, Speculative Markets and the Effectiveness of Price Limits, Journal of Economic Dynamics and Control (2003) (discussing when price limits can be welfare-improving).

[1673] Dai, Jin and Liu, Illiquidity, Position Limits, and Optimal Investment (working paper 2009); Edirsinghe, Naik, and Uppal, Optimal Replication of Options with Transaction Costs and Trading Restrictions, Journal of Financial and Quantitative Analysis (1993); Shleifer and Vishney, The Limits of Arbitrage, Journal of Finance (1997).

[1674] Schulmeister, Technical Trading and Commodity Price Fluctuations (working paper 2012).

[1675] Morris, Speculative Investor Behavior and Learning, Quarterly Journal of Economics (1996); Kyle and Wang, Speculation Duopoly with Agreement to Disagree: Can Overconfidence Survive the Market Test?, Journal of Finance (1997); Leitner, Inducing Agents to Report Hidden Trades: A Theory of an Intermediary, Review of Finance (2012); Sockin and Xiong, Feedback Effects of Commodity Futures Prices (working paper 2012); Froot, Scharfstein, and Stein, Herd on the Street: Informational Inefficiencies in a Market with Short Term Speculation (working paper 1990) (theoretical paper discussing herding); Dicembrino and Scandizzo, The Fundamental and Speculative Components of the Oil Spot Price: A Real Option Value (working paper 2012).

[1676] Basu and Gavin, What Explains the Growth in Commodity Derivatives?, Federal Reserve Bank of St. Louis (2011), provides an excellent analysis of the factors driving rapid increases in volume in commodity derivatives trading. *See* also Easterbrook, Monopoly, Manipulation, and the Regulation of Futures Markets, Journal of Business (1986); Pirrong, Squeezes, Corners, and the Anti-Manipulation Provisions of the Commodity Exchange Act, Regulation (1994).

[1677] For example, a CME Group white paper, Excessive Speculation and Position Limits in Energy Derivatives Markets (undated), lacks empirical data or other economically valid supporting analysis. It also uses confusing terminology. For example, CME quotes a Wall Street Journal survey of economists, which in turn summarily concludes: ''[t]he global surge in food and energy prices is being driven primarily by fundamental market conditions, rather than an investment bubble.'' *Id.* at p.5. Even economists who find some price impact from outsized speculative positions would not disagree that, in the main, prices remain determined ''primarily'' by market fundamentals. And many of these economists finding price impact would not ascribe the result to an ''investment bubble.''

[1678] Frenk and Turbeville, Commodity Index Traders and the Boom/Bust Cycle in Commodities Prices (Better Markets 2011).

[1679] *See id.* at 8–9 for a description of the mechanics of the roll. *See also* Mou, Limits to Arbitrage and Commodity Index Investment: Front-Running the Goldman Roll (working paper 2011).

[1680] *See id.* at 5–6 for a description of contango, an upward-sloping forward price curve for a commodity. Market participants may view contango as evidence that commodity prices will increase in the future.

[1681] *Id.* at 2. *See id.* at 4 (focusing on crude oil and wheat price spreads before, during, and after the role from January 1983 to June 2011).

[1682] Otherwise, other market participants may assume that the rolling activity reflects an informed trader reacting to market fundamentals and the roll could well impair the price discovery function of the commodities market. See Urbanchuk, Speculation and the Commodity Markets, at p. 12 (working paper 2011) (''traders can misinterpret an index inflow as a bullish statement by a trader with superior information''). While not every large institutional trader has to ''sunshine,'' those that announce their rolling timing in their prospectus are bound by SEC rules to follow their prospectus procedures.

[1683] *See* Parsons, Black Gold & Fool's Gold: Speculation in the Oil Futures Market, at 99–101, Economia (2009) (discussing crude oil market economics that explain why crude oil futures prices are sometimes in contango); id. at 101 (''Although oil futures fluctuate between backwardation and contango, on average they have been backwarded'').

[1684] *See, e.g.,* Cooper, Excessive Speculation and Oil Price Shock Recessions: A Case of Wall Street ''Déjà vu all over again'', Consumer Federation of America (2011); Berg, The Rise of Commodity Speculation: From Villainous to Venerable (UN FAO 2011); Eckaus, The Oil Price Really Is a

b. Senate Reports

i. Senate Report on Oil and Gas Prices

The U.S. Senate staff report on oil prices concludes that increased participation by speculators in the energy commodity futures markets has had an effect on energy prices.[1685] Other survey pieces assert that market fundamentals fully explain commodity price spikes.[1686] These survey articles do not present rigorous statistical models to support their competing conclusions.

The Senate report points out that fundamental supply and demand were factors increasing energy prices.[1687] But it determines that these factors ''do not tell the whole story.'' [1688] It asserts that the large purchases of crude oil futures contractors by financial speculators ''have, in effect, created an additional demand for oil. . . .'' [1689] The report acknowledges that the price effect is ''difficult to quantify,'' and cites unspecified analysts on estimated price impact.[1690]

But in the general economics of the futures market, demand for futures contracts does not necessarily increase the demand for, or price of, the physical commodity. In the particular context of the crude oil markets, as discussed above, demand for ''paper oil'' may not directly translate into spot price impact due to storage economics.[1691]

Regarding price effect, the Senate report relies on anecdotal evidence because of the difficulty in quantification. The Senate report cites reports from energy industry participants that financial speculators have caused the price of oil to rise.[1692] The report also acknowledges that analyses of the effect of speculation on these energy markets have reached divergent conclusions.[1693]

The Senate Report does not analyze how position limits would ameliorate the problem it identifies. While not all the speculators referenced in this report would be affected by a position limit rule, the Senate Report does list Brian Hunter, then a trader in natural gas for Amaranth Advisors hedge fund, among the top 2005 energy traders.[1694] These reports, which include factual recitation and anecdotal evidence, contain no models or methods that can be audited by economists.

ii. Senate Report on Wheat

The Senate staff report concerning wheat [1695] surveys economic literature and certain market data, but, like the Senate Report on oil and gas prices, this report does not use statistical or theoretical models to reach an economically rigorous conclusion. The Senate wheat report does include anecdotal evidence: Virtually all of the commercial traders interviewed by the Senate staff ''identified the large presence of index traders in the Chicago market as a major cause'' of a problem with price convergence in wheat in 2008.[1696] The staff report states that the demand for wheat futures contracts has itself increased the price of wheat futures contracts relative to the cash market for wheat:

> These index traders, who buy wheat futures contracts and hold them without regard to the fundamentals of supply and demand in the cash market for wheat, have created a significant additional demand for wheat futures contracts that has as much as doubled the overall demand for wheat futures contracts. Because this significant increase in demand in the futures market is unrelated to any corresponding supply or demand in the cash market, the price of wheat futures contracts has risen relative to the price of wheat in the cash market. The very large number of index traders on the Chicago exchange has, thus, contributed to ''unwarranted changes'' in the prices of wheat futures relative to the price of wheat in the cash market. These ''unwarranted changes'' have, in turn, significantly impaired the ability of farmers and other grain businesses to price crops and manage price risks over time, thus creating an undue burden on interstate commerce. The activities of these index traders constitute the type of excessive speculation that the CFTC should diminish or prevent through the imposition and enforcement of position limits as intended by the Commodity Exchange Act.[1697]

However, there are other reasons that can also explain this 2008 price divergence. The CME wheat contract was poorly designed to account for the cost of storage, and this has been cited as a reason for the price divergence between futures and spot wheat contracts during the 2008 time period. When CME revised its wheat contract, this price divergence dissipated.[1698]

That said, the more formal statistical studies discussed throughout establish rationales for concern with index traders that are grounded in more rigorous economic reasoning. There are circumstances when a large volume of financial index investment flows may causes market prices to deviate from fundamental values.[1699] Alternatively, a

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Speculative Bubble, at p.8, MIT Center for Energy and Env'l Research (2008) (''there is no reason based on current and expected supply and demand that justifies the current price of oil''); Parsons, Black Gold & Fool's Gold: Speculation in the Oil Futures Market, Economia (2009) (explaining why, on a theoretical level, the absence of large crude oil inventories does not preclude a crude oil price bubble); Tokic, Rational destabilizing speculation, positive feedback trading, and the oil bubble of 2008, Energy Economics (2011) (survey with theoretical model adjunct). *See also* Urbanchuk, Speculation and the Commodity Markets, at 8–9 (working paper 2011) (observing that the share of corn futures held by commercial traders has fallen from more than 70 percent in January 2005 to about 40 percent in August 2011); id. at 12 (arguing that speculators are a major factor behind the sharp increase in the level and volatility of corn prices in 2011 because ''traders can misinterpret an index inflow as a bullish statement by a trader with superior information''); Inamura, Kimata, et al., Recent Surge in Global Commodity Prices (Bank of Japan Review March 2011) (contending that global monetary policies have tended to boost commodity prices).

[1685] The Role of Market Speculation in Rising Oil and Gas Prices: A Need to Put the Cop Back on the Beat, Permanent Subcommittee on Investigations of the U.S. Senate Committee on Homeland Security and Governmental Affairs at pp. 19–32 (June 27, 2006) (''Senate Report on oil and gas prices'').

[1686] *See, e.g.,* Plante and Yücel, Did Speculation Drive Oil Prices? Futures Market Points to Fundamentals (Federal Reserve Bank of Dallas Econ. Ltr. Oct. 2011) (if speculating were the cause of crude oil spokes, it would ''leave telltale signs in certain data, such as inventories'').

[1687] The Role of Market Speculation in Rising Oil and Gas Prices: A Need to Put the Cop Back on the Beat at p.12.

[1688] *Id.* at 13.

[1689] *Id.*

[1690] *Id.* at 14. *See id.* at 23.

[1691] *See* Parsons, Black Gold & Fool's Gold: Speculation in the Oil Futures Market, Economia (2009); n.1491, supra. *Contra* Senate Report on oil and gas prices at 13 (''As far as the market is concerned, the demand for a barrel of oil that results from the purchase of a futures contract by a speculator is just as real as the demand for a barrel that results from a purchase of a futures contract by a refiner'').

[1692] Senate Report on oil and gas prices at 22 (claiming that financial investors have created ''runaway demand''), 24 n. 128 (traders assert cross-market arbitrage in energy between futures and over-the-counter markets may be driving speculative pressure).

[1693] *Id.* at 24, 26 (observing that Goldman Sachs issued a report concluding that speculators were impacting crude oil prices, peaking at $7 per barrel in the spring of 2004, and that industry traders and CFTC staff in a 2005 analysis disagreed as to whether a speculative price was caused by financial speculators).

[1694] *Id.* at p.30.

[1695] Excessive Speculation in the Wheat Market, Majority and Minority Staff Report, Permanent Subcommittee on Investigations of the U.S. Senate, Committee on Homeland Security and Governmental Affairs (June 24, 2009).

[1696] Excessive Speculation in the Wheat Market at 11–12.

[1697] *Id.* at 12.

[1698] See supra note 1547. When CME revised its wheat contract, this price divergence dissipated. The futures wheat contract, at expiration, had a valuable real option to store the wheat at a below-market price. This may have been a primary reason why it was more valuable at expiration than spot wheat.

[1699] *See* Aulerich, Irwin, and Garcia, Bubbles, Food Prices, and Speculation: Evidence from the CFTC's Daily Large Trader Data Files, at pp.2–3, NBER Conference on Economics of Food Price Volatility (2012) (summarizing that this could happen when (1) the futures market is insufficiently liquid to absorb large order flow, (2) the index traders are in effect noise traders who make arbitrage risky, or (3) large order flow on the long

Continued

classical economist would argue that prices are still determined by supply and demand, but that the aggregate risk appetite for financial assets affects the demand for commodities through a more complicated process than previously envisioned.

For reasons similar to the Senate Report on Oil and Gas Prices, the Senate Report on Wheat is less useful to an academic than it may be to policymakers.

iii. Senate Report on Natural Gas

A similar analysis applies to the Senate report on natural gas, *Excessive Speculation in the Natural Gas Market.* The report, which focuses at length on Amaranth's natural gas trading, does not include a statistical analysis of empirical data and, as the minority report notes, some '' facts . . . support the conclusion that Amaranth's trading activity was the primary cause of'' natural gas price spikes,'' but other facts point to market fundamentals.[1700]

The report does argue that if Amaranth's large-scale speculative trading was causing ''large jumps in the price differences'' and prices that were ''ridiculous,'' [1701] the current regulatory regime would be unable to prevent this price disruption.[1702]

4. Comments That Consist of Economic Studies or Discuss Economics in Depth

Several comment letters perform substantial summary analysis of other economic studies bearing on position limits, present original economic analysis or formal economic studies. These submissions thus warrant individual analysis. The following submissions are summarized and analyzed in this section:

(A) the February 10, 2014, comment letter by Markus Henn of World Economic, Ecology & Development, including, as an attachment, a November 26, 2013, list of studies entitled ''Evidence on the Negative Impact of Commodity Speculation by Academics, Analysis and Public Institutions'' (''Henn Letter''); [1703]

(B) the analysis of Philip K. Verleger of the economic consulting firm PKVerleger LLC, attached as Annex A to the February 10, 2014 comment letter by the International Swaps and Derivatives Association (ISDA) and the Securities Industry and Financial Markets Association (SIFMA) (''2/10/14 ISDA/ SIFMA Comment Letter'');

(C) the analysis of Craig Pirrong, Professor of Finance at the University of Houston Business School, attached as Annex B to the 2/10/14 ISDA/SIFMA Comment Letter;

(D) two studies by Sanders and Irwin, *The ''Necessity'' of New Position Limits in Agricultural Futures Markets: The Verdict from Daily Firm-Level Position Data* (working paper 2014), and *Energy Futures Prices and Commodity Index Investment: New Evidence from Firm-Level Position Data* (working paper 2014);

(E) two studies by Hamilton and Wu, *Effects of Index-Fund Investing on Commodity Futures Prices,* International Economic Review, Vol. 56, No. 1 (February 2015), and *Risk Premia in Crude Oil Futures Prices,* Journal of International Money and Finance (2013) (submitted as second paper in the same electronic comment submission); and

(F) materials that CME Group submitted for inclusion in the administrative record, include 3 sets of materials submitted on March 28, 2011 (first set, second set, and third set); an undated CME study on conditional spot-month limits; and a CME Group's white paper, *Excessive Speculation and Position Limits in Energy Derivatives Markets.*[1704]

a. The Markus Henn List of Studies

Markus Henn's February 10, 2014, comment letter acknowledges that there is an ongoing debate about whether speculators can dominate a marketplace and exacerbate market volatility and market prices. He nonetheless asks the Commission to take into account a list of studies he submits with his letter. He then presents numerous economic studies as well as media articles.

As a group, this list of studies, opinion pieces, and news articles documents the existence of concern and suspicion about large speculative positions in commodity markets. Many of the studies cited by the Henn Letter look for evidence of financialization and in this sense suffer from interpretational bias.[1705] As a group, these opinion pieces and studies do not consistently seek alternative explanations for their conclusions. As Markus Henn acknowledges in his cover letter, these papers are part of an ongoing debate among economists, not conclusive evidence of the harmful effects of excessive speculation.

Three of the most persuasive papers, persuasive insofar as they employ well-accepted, defensible, scientific methodology, document and present facts and results that can be replicated, and are on point regarding issues relevant to position limits, cited in the Henn Letter involve the crude oil market during the financial crisis: Singleton, *Investor Flows and the 2008 Boom/Bust in Oil Prices* (March 23, 2011 working paper); [1706] Hamilton and Wu, *Risk Premia in Crude Oil Futures Prices,* Journal of International Money and Finance (2013) (an earlier working paper version is cited by Henn); and Hamilton, *Causes and Consequences of the Oil Shock of 2007–2008,* Brookings Paper on Economic Activity (2009). The first two conclude that there is a statistical link between the volume of speculative positions and a component of price, risk premium, at least for some commodities in some timeframes. Hamilton's *Causes and Consequences of the Oil Shock of 2007–2008* concludes that the oil price run-up was caused by strong demand confronting stagnating world production, but the price collapse was perhaps not driven by fundamentals.

side of the market is seen erroneously as traders taking bullish positions based on valuable information about market fundamentals). *See id.* at pp.3–4 (observing contrasting findings depending on impact of index trading depending on liquidity of the agricultural commodity market); Singleton, Investor Flows and the 2008 Boom/Bust in Oil Prices, at 5–8 (March 23, 2011 working paper) (learning about economic fundamentals with heterogeneous information may induce excessive price volatility, drift in commodity prices, and a tendency towards booms and busts); Tang and Xiong, Index Investment and Financialization of Commodities, at p.30, Financial Analysts Journal (2012) (''the price of an individual commodity is no longer simply determined by its supply and demand''); *id.* at 29–30 (''Instead, prices are also determined by a whole set of financial factors such as the aggregate risk appetite for financial assets'').

[1700] *Id.* at 135 (while price of natural gas declined after Amaranth's demise, ''this alone does not prove Amaranth's ability to elevate prices above supply and demand fundamentals'').

[1701] *Id.* at 3.

[1702] *Id.* at 3 (NYMEX exchange did not have routine access to Amaranth's trading positions on ICE, and therefore NYMEX could not have a complete and accurate view of whether ''a trader's position . . . is too large.'' In addition, there were no accountability limits on the ICE exchange).

[1703] *See* Letter from Markus Henn, World Economic, Ecology & Development, to CFTC (Feb. 10, 2014), available at *http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=59628&SearchText=henn. See also,* Markus Henn, Evidence on the Negative Impact of Commodity Speculation by Academics, Analysis and Public Institutions, (Nov. 26, 2013), available at *http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=59628&SearchText=henn.*

[1704] The CME white paper, while technically not submitted formally by CME in the administrative record, warrants individualized analysis. It is cited in the Commission's December 2013 Position Limits Proposal; it is posted on the CME Group's Web site; and it is cited in arguments by such commenters as MFA. (MFA February 9, 2014 comment letter at 11–12, n.26).

[1705] *Id.*

[1706] Markus Henn cites the 2011 version of the Singleton paper, which is the only version of this paper in the administrative record. A subsequent May 2012 version is available from Professor Singleton's Stanford Web site at *http://web.stanford.edu/~kenneths/.*

b. Verleger's Analysis, Attached to ISDA/SIFMA Comment Letter

Philip K. Verleger provided an analysis as a retained expert for ISDA. Annex A to the 2/10/14 ISDA/SIFMA Comment Letter. He contends, without quantitative modelling or empirical evidence, that in the energy markets ''unwarranted price fluctuations'' have historically been due to ''confluence of contributing factors'' such as weather, geopolitical events, or changes in industry structure. 2/10/14 ISDA/SIFMA Comment Letter, Annex A at pp. 2–3. In passing, he opines, without analysis or citation, that the high energy prices in 2008 ''are attributable to environmental regulation.'' *Id.* Verleger also asserts that his expertise is in the energy markets, yet opines (contrary to many comment letters from other energy market participants) that the energy markets are ''subject to conditions and dynamics'' of other commodity markets. *Id.* at p.2. For these reasons, we view Verleger's analysis as weak and conclusory and lacking in economic rigor and empirical data.

By way of further example, Verleger contends that if the position limits rule had been in effect in 2013, oil prices would have been $15 per barrel higher and the cost to American consumers would have been roughly $100 billion. Annex A at p.3. He provides no quantitative reasoning in support of these numbers.[1707]

Verleger also asserts that exploration for sources of energy has resulted in a large increase in oil supply in recent years, and states that these companies use swaps and futures to hedge their position. *Id.* at p.7. He then summarily asserts that independent companies exploring for and developing oil and gas production would ''not have achieved this success without hedging'' and that hedging would not have occurred if the Commission's position limits had been in place. *Id.* at p.8. Verleger overlooks several critical facts.

First, companies actively engaged in oil and gas exploration might either qualify for bona fide hedging treatment or fall within the position limit. As to non-spot month limits, Verleger concedes that ''it may be argued that the initial non-spot month position limits are high enough (109,000 contracts for crude as an example)'' to avoid liquidity impacts. *Id.* at 12.[1708]

Second, he argues that these exploration companies have ''benefited indirectly because passive investors such as retirement funds have taken long positions in commodities through the swap markets,'' and suggests that with position limits there would be an absence of non-commercials to take positions opposite oil and gas development companies. *Id.* at 9. To the contrary, with the Commission's disaggregation exemption for managed funds (the independent account controller exemption), there is no basis to believe that there will be a shortage of long positions in the market. He presents no empirical evidence to support his thesis that position limits could thus ''adversely affect[ ] investment in the oil and gas industry.''[1709]

Third, the way energy derivatives markets work, if there is demand on the short side of the market, this may create liquidity on the long side of the market to transact with at some price. Verleger himself notes the diversity of market participants—commodity-based exchange-traded funds, hedge funds, retirement funds, and the like—and does not document that the exclusion of a particular long would reduce liquidity from the marketplace. For example, commodity-based exchange-traded funds trade intermediate long positions for their investors, and if the funds themselves could not take long positions in the market, there is no reason to assume that the investors might through other vehicles take long positions. Verleger has an expressed fear, not an analysis, that liquidity in markets will be harmed by position limits.[1710]

c. Pirrong's Analysis, Attached to ISDA/SIFMA Comment Letter

Professor Pirrong agrees that the nation's commodity markets have been subject to significant and disruptive corners and squeezes, such as the Hunt Silver episode of 1979–1980.[1711] He concedes that the ''ability of position limits to prevent corners and squeezes could provide a justification for application of these limits during the spot month,'' at least in theory.[1712] He concedes that in theory there is such a thing as ''sudden and unwarranted price fluctuations.''[1713] Subject to these concessions, Pirrong opposes many aspects of the rule. Overall, Pirrong argues that position limits are an undesirable solution to an economic problem that has not been proven to exist.[1714] We analyze below his objections only when and to the extent that they rest on economic arguments.

i. Amaranth and the Possible Utility of Position Limits in Non-Spot Months

Pirrong states that the possibility of a corner or a squeeze ''provides no justification of the necessity of imposing position limits outside the spot month.''[1715] Pirrong argues that Amaranth's market activity in 2006 is not evidence of the utility of position limits in the non-spot month. *Id.* at p.2, ¶ 7. In this context, Pirrong discusses corners and squeezes as the rationale for non-spot month position limits. *Id.* However, the Commission's December 2013 Position Limits Proposal discusses rationales other than corners and squeezes: Economic factors such as outsized market power, disorderly liquidation, and the ability to manipulate prices.

In the context of non-spot month position limits, Pirrong focusses just on corners and squeezes. If that were the only regulatory concern, his analysis on this, *see id.* at ¶¶ 27–30, would be largely correct. Many traders exit futures contracts before the spot month because they are there for the exposure, for price risk transfer, not to make or take delivery.

One key reason why ETFs ''sunshine-trade'' their rolls—announcing in their prospectus when they will roll—is because rolling these large positions in non-spot months can have a price impact, apart from corners and squeezes.[1716]

A good example of the risk of price impact in non-spot months from outsized positions, apart from corners

[1707] Verleger argues that limits in the non-spot month would have an especially chilling effect, ''very likely leading to, among other things, higher energy prices;'' and that position limits should not apply to cash-settled markets because traders holding cash-settled contracts do not have any ability to influence the physical market prices of commodities. *Id.* at 2–3. Pirrong also makes these arguments but provides further analysis, so we discuss this critique in subsection C below.

[1708] *See* Berg, The Rise of Commodity Speculation: From Villainous to Venerable, at p.263 (UN FAO 2011) (former CBOT trader suggests that spot month limit positions should be in place for at least a few days in the non-spot months to lesson price distortions from the roll).

[1709] *Id.*

[1710] *See, e.g.,* id. at 12 (after observing that non-spot month limits are high enough to perhaps not impact the market, stating that non-spot limits will ''adversely affect the ability of commercial participants to use some futures market'').

[1711] CL–ISDA/SIFMA–59611, Annex B, at 2, ¶¶ 6–9.

[1712] *Id.* at ¶ 7.

[1713] *Id.* at 6, ¶ 27.

[1714] *Id.* at pp. 3–10.

[1715] CL–ISDA/SIFMA–59611, Annex B, at p.2.

[1716] Sanders and Irwin, The ''Necessity'' of New Position Limits in Agricultural Futures Markets: The Verdict from Daily Firm-Level Position Data, at p.19 (working paper 2014) (preannounced trades can have a ''sunshine trading'' effect of increasing liquidity and lowering trading costs). *See, e.g.,* Frenk and Turbeville, Commodity Index Traders and the Boom/Bust Cycle in Commodities Prices (Better Markets 2011) (very large institutional players rolls have had a temporary price impact that is expensive to the ETF investors).

and squeezes, is Amaranth. Amaranth's position was so large that it may have impacted price by virtue of its outsized market position in not just the spot month, but other months. Amaranth may have influenced prices not just upon liquidation, not just when banging the close in the spot month, but also well before then, according to a congressional study cited in the Commission's December 2013 Position Limits Proposal.[1717]

An economist could argue that because the commodity futures price should reflect all demand, Amaranth's very large positions in the non-spot month was appropriately incorporated in market prices. After all, at a given point in time and price, demand is defined as the quantity desired by all those who are willing and able to hold a commodity futures position. Prof. Pirrong's approach does conceive of the possibility that outsized market power in the non-spot month or the price impact of Amaranth's positions could have deleterious effects on the marketplace. From a classical economical perspective, Amaranth's outsized market position in the non-spot months is just an input into price demand.

However, outsized market power may have economic outcomes that are undesirable. Outsized market power permits a player to do more than ''bang the close,'' and Amaranth's natural gas trading is an example of this. One could influence prices in the swaps market through such aggregation of market powers or one could manipulate related markets. Amaranth's exercise of market power may have been real and substantial. Even after it left the natural gas market, its activities may have left a lasting price effect. That is, prices of the underlying commodity, natural gas, may have been higher when Amaranth was in the market (including in the non-spot months), and prices were substantially less for a substantial time period after Amaranth left the market.[1718] Pirrong's discussion of Amaranth does not address this economic history or its possible relevance to non-spot position limits. Although Pirrong criticizes the Commission for not engaging in a ''rigorous empirical analysis'' of Amaranth (2/10/14 ISDA/SIFMA Comment Letter, Annex B, at p.2, ¶ 10), the establishment of outsized market power in economics is more straight forward in the case of Amaranth. The question is whether the disappearance of an Amaranth from the market with its formerly outsized position led to a significant decline in price.

By focusing simply on Amaranth's activities in the spot month, Prof. Pirrong does not discuss the potential for harm arising from Amaranth's outsized positions in the non-spot month. If someone is exerting market power, they can cause a negative externality for other purchases of natural gas if they, for example, bid up the price of natural gas. A higher price for a natural gas purchaser due to another entity's trading may simply be an example of a healthy market at work. However, there is definite harm to purchasers of natural gas if the price they pay is higher for reasons that are associated with another market participant's price influence though the exertion of market power.

Pirrong does not provide a direct factual rebuttal to the Senate investigative report finding that Amaranth's speculative activity affected overall price levels in natural gas. He argues that the Commission's reliance upon a Senate investigatory report would not be ''accepted as evidence of causation in any peer reviewed academic work.'' [1719] *Id.* at 2, ¶ 9. Prof. Pirrong is correct that the Commission has not, in the case of Amaranth, shown causation: That it was Amaranth's departure from the markets that caused the natural gas price decline in substantial part, as opposed to confounding factors (such as, in the case of natural gas, evidence that the upcoming winter would be warmer than expected). However, proof of causation is not required for publication in peer reviewed journals in a case such as this.

To establish evidence of causation, one would need a theoretical model and empirical evidence to support it. There have been peer-reviewed studies on Amaranth such as one cited in the Commission's December 2013 Position Limits Proposal.[1720] That study observed that not just a Senate investigatory committee, but one of the exchanges that Amaranth was trading on, was alarmed by their exercise of market power in months prior to the spot months. The New York Mercantile Exchange (NYMEX) on August 9, 2006: [1721]

> called Amaranth with continued concern about the September 2006 contract and warned that October 2006 was large as well and they should not simply reduce the September exposure by shifting contracts to the October contract. In fact, by the close of business that day, Amaranth increased their October 2006 position by 17,560 positions and their ICE positions by 105.75

This study documents that even though many of the Amaranth positions were not with NYMEX, and instead with ICE, these positions were extremely large relative to the average daily trading volume of the largest natural gas futures exchange. ''In some cases, the positions are hundreds of times the 30-day average daily trading volume.'' [1722]

Pirrong also argues as a normative matter that the costs exceed the benefits. While he concedes that it is ''plausible'' that a sudden liquidation of a large position by a trader facing distress'' could ''cause sudden and unwarranted price fluctuations,'' he argues that there is ''no evidence that this problem occurs with sufficient frequency, or has sufficiently damaging effects, to warrant continuously imposed constraints on risk transfer.'' *Id.* at 6, ¶ 27. The Commission considers the costs and benefits formally elsewhere in this release.

ii. The Possible Harms of Corners and Squeezes

Pirrong also questions the extent of harm associated with activities such as the Hunt brothers. 2/10/14 ISDA/SIFMA Comment Letter, Annex B, at pp. 2–3. He downplays the harms of corners and squeezes. *Id.* at ¶¶ 11–12, 38–43.

Prof. Pirrong is incorrect in asserting that the Commission's view was groundless. In the December 2013 Position Limits Proposal, the Commission did ground its concern about outsized speculative positions in particular examples. The Commission did present evidence of inefficient resource allocation with respect to the Hunt brothers. It is as much a public

[1717] There have been other examples of price manipulations that extended over a period of months. See CFTC staff, A Study of the Silver Market, Report To The Congress In Response To Section 21 Of The Commodity Exchange Act, Part One at 2–4, 9–10 (May 29, 1981) (price of silver rose and fell over a period of months, with long futures positions in silver held by members of the Hunt family in the summer and fall of 1979 and prices peaking in late January 1980, and prices falling though the first quarter of 1980); *id.,* Part Two at p.100 (''behavior of silver prices during 1979–80 appears consistent with, but is not entirely explained by, fundamental developments in the silver market over this period''); p.112 (Hunt family acquired actual and potential control of approximately 18 percent of world silver market and stood for delivery on a significant portion of their futures contracts, causing silver prices to rise significantly).

[1718] This observation presumes no other confounding events such as the occurrence of warmer winter. Unfortunately, we do not know whether or not the lower price resulted from the exit of Amaranth, the warmer winter, something else, or some combination of the preceding.

[1719] *Id.* at 2, ¶ 9.

[1720] *See* Ludwig Chincarini, Natural Gas Futures and Spread Position Risk: Lessons from the Collapse of Amaranth Advisors LLC, Journal of Applied Finance (2008).

[1721] *Id.* at p.24.

[1722] *Id.* at p.22.

policy matter as an economic matter how position limits fare as a solution to the question of these negative externalities. Even if one assumes away the existence of market imperfections, as Pirrong does, one is still left to contend with the consequences of what Pirrong assumes to be natural market events. In the case of the Hunt brothers, the Commission gave multiple examples of negative externalities in the broader economy. People sold their silverware which was melted down into silver bars. A photo supply company dependent on silver supply went out of business.[1723]

Pirrong's assumption that persons act optimally at any given moment does not mean, across time, that resources have been allocated efficiently. While much of economic analysis is static, dynamic effects over time can have inefficient allocation of resources, intertemporally. It may have been optimal for a possessor of silverware to melt down their silver into silver bars during the Hunt silver market disruption, but just a few months later a possessor of silverware would likely prefer silverware to silver bars. *See* Pirrong's *Manipulation of the Commodity Futures Market Delivery Process,* at p. 383, Journal of Business (1993) (futures market manipulations ''distorts prices and creates deadweight losses;'' ''causes shorts to utilize real resources to make excessive deliveries;'' and ''distorts consumption'').

Pirrong thus errs in asserting that the Commission does not provide an ''empirical basis'' for ''inefficient allocation of resources.'' 2/10/14 ISDA/SIFMA Comment Letter, Annex B, at p.3.

iii. Claim That the Spot-Month Limits Are Arbitrary

Pirrong claims that spot month limits are set too low at 25 percent of deliverable supply. *Id.* at p.8, ¶¶ 38–40. He contends that a single long trader has to control over 50 percent of deliverable supply to perfect a corner. *Id.* at ¶ 40. He is incorrect. Assuming, quite reasonably, that long commercials are going to stay in the market and consume, because it would be very expensive for them to leave the market, a certain percentage of deliverable supply is ''locked up'' in this sense. For example, a natural gas utility needs to deliver natural gas for its customers to heat their homes (among other things) and would therefore still take delivery of a substantial percentage of the deliverable supply of natural gas.

Pirrong says that ''[f]ive or more perfectly colluding traders each with positions at the 25 percent level might be able to manipulate the market.'' *Id.* at p.8, ¶ 41. However, these five traders do not all need to collude in order to permit one of them to manipulate price. Some of these traders may simply be those who value the commodity highly, much higher than the market price, and therefore will not let go of their contractual right to delivery. Such commercials may be willing to stay and pay a higher price, even when a corner is in effect, because the cost, for example, of not providing natural gas to customers to heat their homes is substantially more.

Many exchanges, including CME, set position limits lower than 25 percent. It is hard for Pirrong to argue that 25 percent is excessively low when it is higher than CME limits for all of the 19 CME-traded commodities covered by the proposed CFTC position limits.

Pirrong's final critique of spot month limits is his assertion that application of the same limits to short and long positions is arbitrary. *Id.* at p.9, ¶¶ 42–43. The reasons he gives for this are problematic and not well-developed. Pirrong states that for storable commodities, manipulation by long traders is more likely than with short traders. *Id.,* ¶ 42. It may well be more difficult to manipulate price through a corner or squeeze as a short because there is generally a fixed limit for deliverable supply (unless one creates the impression that there is more deliverable supply than there is). Moreover, shorts may well have a bona fide hedging exemption anyway. However, for shorts as well as longs, position limits help to ensure an orderly exit and a smoother delivery process. For example, a short trader with a large position might take a partially offsetting long position in an illiquid market in the spot month; this might cause unwarranted price volatility due to the price impact of establishing the offsetting long position.

Pirrong criticizes the depth of the Commission's basis for treating short and long positions symmetrically, he also does not suggest an alternative or explain how a proper ratio should be calculated.[1724]

iv. Whether Position Limits Cause Economic Harm

Pirrong contends that commodity ETFs, pension funds, and other ''real money'' investors would be harmed by position limits and that this is unfair because not all such market participants impose the same risks. 2/10/14 ISDA/SIFMA Comment Letter, Annex B, at pp.3–4, ¶¶ 16–18. The claim that it is ''unfair'' to impose limits on all market players uniformly is a policy argument, not an economic argument.

d. Hamilton/Wu Papers on Risk Premia and Effects of Index Fund Investing

Professors James Hamilton and Jing Cynthia Wu of the University of California at San Diego and University of Chicago Business School, respectively, authored a well-executed set of papers (well-executed because they used reasonably defensible models with relatively transparent assumptions and data sources) that examine the effect of positions on prices.

Their paper, Hamilton and Wu, *Risk Premia in Crude Oil Futures Prices,* Journal of International Money and Finance (2013), is a well-reasoned explanation for how outsized speculative futures positions could impact risk premium, the return for accepting undiversifiable risk, a component of the return of holding a commodity futures contract. Examining the crude oil futures market, they find that crude oil risk premia fundamentally changed in response to financial investor flows into the crude oil market. *Id.* at p.31.

Hamilton and Wu found that, for crude oil futures, risk premiums, post-2005, were smaller than they were in the pre-2005 sample. This study contains an important conclusion founded in the interplay of positions and prices in the crude oil markets:

> While traders taking the long position in near contracts earned a positive return on average prior to 2005, that premium decreased substantially after 2005, becoming negative when the slope of the futures curve was high. This observation is consistent with the claim that historically commercial producers paid a premium to arbitrageurs for the privilege of hedging price risk, but in more recent periods financial investors have become natural counterparties for commercial hedgers.

Hamilton and Wu, *Risk Premia in Crude Oil Futures Prices,* at p.10, Journal of International Money and Finance (2013).

Their paper tests the idea that risk premia have been bid down by long, speculative investments in the crude oil market. That is, they test the idea that the futures price has become higher as

[1723] December 2013 Position Limits Proposal 78 FR at 75680, 75689.

[1724] Pirrong argues that the Commission's cost-benefit analysis fails to identify, let alone analyze, important potential costs. 2/10/14 ISDA/SIFMA Comment Letter, Annex B, at 4–6. The Commission addresses all commenter criticisms in the cost-benefit section of this release. Pirrong also argues that the Commission's bona fide hedging exemptions are unnecessarily narrow and critiques the Commission's decision to establish different position limits for cash-settled (as opposed to delivery-settled) contracts. The Commission addresses such comments in the relevant sections of this release.

it has been bid up by long speculators, so the return from holding the long futures contract has been lowered. In theory, this phenomenon would make hedging cheap for the short side of the market, but would also increase the price of the futures, all else being equal.

Hamilton and Wu use a two-factor model for price: The futures contract price less the rational expectation of the futures price equals the risk premium, the component of price associated with holding the price risk of the futures contract. A commodity that is more likely to be affected by long passives in this way is crude oil, because (1) crude oil as a commodity dominates these indices—substantial portion of the GSFI for example; (2) the economics of storage.

All else being equal, if outsized market positions affect price, we should expect risk premium to be the component of price that would be affected when market participants take outsized positions. That is because risk premium is a return for taking on undiversifiable risk. A risk premium does not include that portion of risk that can be easily diversified through other instruments. Through the workings of market, a participant who takes on a price exposure will expect to be compensated through a premium for bearing this risk. For a futures commodity contract, there are many components of the return, and the risk premium is only one of them. It can be a fairly small component, although the fraction depends on the commodity and other the market conditions.

Hamilton and Wu construct a theoretical price return: The return of holding a long futures contract based on a rational expectations model. Hamilton and Wu, *Risk Premia in Crude Oil Futures Prices,* Journal of International Money and Finance (2013). Their risk premium is the difference between futures return and theoretical price return. They find that risk premiums for crude oil decreased over time and became more volatile. While Hamilton and Wu listed many assets in the paper's introductory discussion of the theoretical model, in their empirical analysis they use two factors, that involve only futures price data. This omission fails to take into account potentially relevant data about the level of various commodities in storage [1725] and observations about other financial assets.[1726] Consequently, there may be some disconnect between their theoretical and their empirical model. This may mean that the study's theoretical price return is on less sound theoretical footing than it may first appear. Nevertheless, the benchmark rational expectation return may still be a suitable approximation.

In a second paper, *Effects of Index-Fund Investing on Commodity Futures Prices, International Economic Review,* (February 2015), Hamilton and Wu were able to replicate Singleton's result for the crude oil market during the 2006–2009 period. They found an effect from speculative positions of index investors on risk premium in crude oil.[1727] Hamilton and Wu also did not find evidence of speculative positions influencing risk premia in crude oil after 2009. Nor did they find evidence that speculative positions affected the risk premia in the agricultural commodities markets. ''Our conclusion is that although in principle index-fund buying of commodity futures could influence pricing of risk, we do not find confirmation of that in the week-to-week variability of the notional value of reported commodity index trader positions.'' *Id.* at p.193; *see id.* at p.195 (no persuasive evidence that changes in index trader positions is related to risk premium in agricultural commodities, whether the data is studied for change on a weekly or 13-week basis). Consequently, they find only limited evidence for a theoretically reasonable version of the Master's hypothesis, *i.e.,* that long speculators bid down the risk premia and as a result induce a higher futures price in various commodity futures markets. ''Overall,'' Hamilton and Wu conclude, their work indicates that ''there seems to be little evidence that index-fund investing is exerting a measurable effect on commodity futures prices.'' *Id.* at p.204 (adding that it is ''difficult to find much empirical foundation for a view that continues to have a significant impact on policy decisions'').

e. Sanders/Irwin on the ''Necessity'' of Limits and Energy Futures Prices

Professors Dwight Sanders and Scott Irwin submitted two working papers: (1) One paper arguing that new limits on speculation in agricultural futures markets are unnecessary; [1728] and (2) a paper on energy futures prices, using high frequency daily position data for energy markets and concluding that there is no compelling evidence of predictive links between commodity index investment and changes in energy futures prices.[1729]

i. The ''Necessity'' of New Position Limits

In Sanders and Irwin, *The ''Necessity'' of New Position Limits in Agricultural Futures Markets: The Verdict from Daily Firm-Level Position Data* (working paper 2014), the authors use price and position data shared by an unnamed large investment company.[1730] They do various statistical analyses to concluding that the large investment company's roll of its position does not have any lasting price impact on the market. The find that the price impact of the roll is, at most, a small and temporary price impact; there is not a day-over-day impact and the impact is smaller than the bid/ask spread.

This result does not disprove, generally, the possibility that the fund's long, speculative positions impact price because it focuses only on one aspect of the fund's trading: Its rolling of positions. The firm data used is from a large commodity index fund that is registered investment company, and such a firm is likely put into their prospectus how they are going to roll their positions. This pre-announcement of when the commodity index fund will roll may dampen the price impact of these particular changes in position. *See* n.1682 and associated text, *supra;* Aulerich, Irwin, and Garcia, *Bubbles, Food Prices, and Speculation: Evidence from the CFTC's Daily Large Trader Data Files, id.* at p.29 (NBER Conference

[1725] Risk premia may vary based on the amount of a commodity in storage at any given time. While discussing storage as a component of risk premia seems overly technical, in many of these papers, including the Hamilton and Wu paper, it might play an import role. One could go long a crude oil futures contract, or one could buy crude oil and storage it. If you do the latter, you could draw down the physical commodity available for near-term use. Also, the storing of the physical commodity has a real option component to it (one can take the crude oil out of storage and consume it relatively quickly). The value of the real option depends on how much society might need crude oil in storage, and that value depends on how much crude oil is stored elsewhere.

[1726] The papers discussed in the financialization section suggest that the returns of financial assets may affect commodity returns and vice versa.

[1727] Professor Kenneth Singleton found evidence that speculative positions Granger-causing risk premium on weekly time intervals during the 2007 to 2009 period when studying the crude oil futures markets. Singleton, Investor Flows and the 2008 Boom/Bust in Oil Prices (March 23, 2011 working paper).

[1728] Sanders and Irwin, *The ''Necessity'' of New Position Limits in Agricultural Futures Markets: The Verdict from Daily Firm-Level Position Data* (working paper 3/13/2014), comment letter at 1–46.

[1729] Sanders and Irwin, *Energy Futures Prices and Commodity Index Investment: New Evidence from Firm-Level Position Data* (working paper 2/17/2014), comment letter at 47–89.

[1730] *Id.* at 4–5. They argue that this dataset will be more comprehensive than the CFTC's commitment of trader data, but they did not test to verify this assumption. They correctly observe that prior work using CFTC data suffers from limitations in the frequency of data and the availability of swaps data. *Id.* at 3, 5.

2012) (firms preannounce their rolls, and thus these position changes can be anticipated by the marketplace and thus lead to less price impact). Sanders and Irwin's result thus is not obviously extensible to any price impact of this large index fund's positions apart from its positions and trading at the time of roll.

This fund did have days of heavy trading, apart from rolling, but Sanders and Irwin did not study the price impact arising from these changes in position. The fund traded cotton contracts representing 5.8% of average daily trading in cotton and wheat trades constituting 3.5% of average daily volume in the MGEX wheat contract. Sanders and Irwin did not attempt to study price impact on these un-announced trades. They stated that because the sizes of the roll transactions are ''larger than changes in outright position,'' ''investigating the impact of rolling on market spreads'' is ''particularly interesting.'' *Id.* at p.10. On the other hand, the non-roll position changes are presumptively not preannounced to the marketplace, so studying this rich dataset for price impacts from those position changes might also be interesting.

This paper by Sanders and Irwin thus has a limitation of scope based on its focus on just the rolling of positions. This large commodity index fund presumptively pre-announced its rolling of positions in its prospectus. However, this leaves open the question of what would be the effect if this same fund did not pre-announce in the future. The analysis by Sanders and Irwin, if credited as true within a reasonable degree of certainty, would address whether regulators should employ position limits prophylactically to diminish the price impact of any future, non-announced rolls. At least prior to sunshine trading of rolls, there is evidence of a price impact associated with rolling. Frenk and Turbeville, *Commodity Index Traders and the Boom/Bust Cycle in Commodities Prices* (Better Markets 2011).[1731]

Moreover, not all large players pre-announce their rolls. The fact that Sanders and Irwin found no price impact with respect to rolls that were (assumedly) pre-announced does not mean that unannounced rolls might be mistaken for informed trading by the marketplace and cause a price impact.[1732]

Despite these limitations in scope, Sanders and Irwin's article is one of the more useful Granger analysis papers for several reasons.

First, it does present a working definition of ''excessive speculation:'' speculation that is ''causing'' price fluctuations that are ''sudden'' or ''unreasonable'' or ''unwarranted.'' Sanders and Irwin correctly state that their ''definition of excessive speculation seemingly excludes speculation that cannot be shown to *cause* price changes. . . .'' *Id.* at p.3. It is important to note, however, that Sanders and Irwin repeatedly use the word ''necessary'' to analyze the desirability of position limits, which elevates the requirements for establishing causation of price fluctuations to a very high level. High quality economic studies often use empirical data, typically the tools of statistics, to achieve reasonable certainty within a specified degree of error.

Second, the data source is a novel and fairly comprehensive data set. It includes both swaps and futures, and encompasses many different commodities. The data does indicate the volume and nature of this large commodity fund's positions in the market place. All positions taken by the firm during the 2007–2012 time period were long positions, not short positions. *Id.* at p.5. The fund's total position size (including futures and swaps) grew from under $4 billion in 2007 to $12 billion in 2011. *Id.*

Third, with respect to the paper's conclusion on rolling of positions, the statistical result of Sanders and Irwin—concluding that there was no price impact from positions—is stronger than many other studies in some respects. Unlike Hamilton and Wu's work on just a component of the return from holding a futures contract (risk premium), Sanders and Irwin consider the entire return from holding the futures contract. They studied data over a long time period. If their model is correct, they have found evidence against (at least their formulation of) the Masters hypothesis. There is a potential concern, however, with their statistical result. The price equation used for their Granger analysis uses both lagged returns and changes in positions. *See id.* at p.16 (''$R_{t-i}$'' are lagged returns and ''Positions'' are changes in position in Equation 5a). To the extent that lagged returns and position changes are correlated with each other, their price equation may mask correlations between price returns and position changes.

ii. Energy Futures Prices

Using the same commodity index fund data, Sanders and Irwin examine energy contracts: Crude oil, heating oil, natural gas, and reformulated blend stock gas (with ethanol added). Sanders and Irwin, *Energy Futures Prices and Commodity Index Investment: New Evidence from Firm-Level Position Data* (working paper 2014). This paper attempts to challenge the findings of an impact on price from positions by Singleton, Hamilton and Wu. Sanders and Irwin contend that their richer data source compels a conclusion that positions in commodity energy markets do not impact price.

This paper also has a potential problem with the price return equation. The equation, *see id.* at p. 15 (Equation No. 7), uses lagged returns and positions to test against a correlation with price. Sometimes they use multiple lagged returns. For example, for their natural gas analysis, they used two sets of lagged returns. *Id.* at p.35 (Table 5). Again, use of lagged returns in the price equation can mask a possible correlation.

Sanders and Irwin argue that their results from a richer data source indicate that Singleton and Hamilton and Wu's results may be ''artifacts'' of poor data. They contend that these authors' use of agricultural data as proxy for energy positions was problematic. *Id.* at p.3. They suggest this may explain the differing results of Singleton, as well as Hamilton and Wu.

But there are other explanations for this difference in results. Singleton, Hamilton and Wu focus on risk premium, not, as Sanders and Irwin do, on price returns. This distinction can be quite important in this context. If positions impact price by impacting risk premium, that effect will not necessarily reveal itself in a study of just price returns. Perhaps more fundamentally, Sanders and Irwin and are asking a

[1731] An example of a study that is, in part, forward-looking, is Cheng, Kirilenko, and Xiong, Convective Risk Flows in Commodity Futures Markets (working paper 2012). The authors use comovement methodology to conclude that in times of distress, financial traders reduce their net long position, causing risk to flow from financial traders to commercial hedgers. *See also* Acharya, Ramadorai, and Lochstoer, Limits to Arbitrage and Hedging: Evidence from the Commodity Markets, Journal of Financial Economics (2013) (decreases in financial traders' risk capacity should lead to increases in hedgers' hedging cost, all else being equal).

[1732] Sanders and Irwin's piece does not directly test the effect of pre-existing position limits in these markets. Examining agricultural markets for whether there can be price impact on positions generally is complicated by the fact that the agricultural markets have been subject to federal position limits since 1920s. On the other hand, in the case of a commodity index fund, they may well not be carrying substantial positions into the spot month, and so even their large source of firm data may not be useful for testing the impact or effectiveness of position limits during the spot month.

slightly different question than Hamilton and Wu or Singleton. Sanders and Irwin are attempting to measure speculative position changes impact on price returns over a long time period, February of 2007 to May 2012. Hamilton and Wu, and also Singleton, use narrower timeframes in their papers and find a component of return, the risk premium, during a narrow time window, during a period of economic stress.

f. CME Group Study Submissions

The CME Group filed in the administrative record several studies and reports on March 28, 2011. It did so in three sets, all filed on March 28, 2011.

In the first set, CME filed: *Tackling the Challenges in Commodity Markets and Raw Materials,* European Commission (2011) (2.2.2011); Issues Involving the Use of the Futures Market to Invest in Commodity Indexes, Government Accountability Office Letter to the Hon. Collin Peterson, Chair, House Committee on Agriculture (June 30, 2009); and Korniotis, *Does Speculation Affect Spot Price Levels? The Case of Metals With and Without Futures Markets,* Working Paper of the Finance and Economic Discussion Series, Federal Reserve Board (2009).

In a second set, CME filed: Stoll and Whaley, *Commodity Index Investing and Commodity Futures Prices,* Journal of Applied Finance (2010); and Irwin and Sanders, *The Impact of Index and Swap Funds on Commodity Markets: Preliminary Results* (OECD Food, Agriculture and Fisheries Working Papers, No. 27 2010).

In a third set, CME filed: Celso Brunetti and Bahattin Büyükşahin, *Is Speculation Destabilizing?* (working paper 2009); Bahattin Büyükşahin and Jeffrey H. Harris, *The Role of Speculators in the Crude Oil Futures Market* (working paper 2009); and Interagency Task Force on Commodity Markets, *Interim Report on Crude Oil* (July 2008).

Finally, CME submitted an undated CME study on conditional spot-month limits and CME Group's white paper, *Excessive Speculation and Position Limits in Energy Derivatives Markets.*

As a group, these studies are not new to the Commission. All of these papers, except the CME undated submission on conditional spot limits and the European Commission publication, were cited by the Commission in its December 2013 Position Limits Proposal and so are covered in the above analysis of various studies.[1733]

Conclusion

Economists debate whether ''excessive speculation'' meaning, as an economic matter, a link between large speculation positions and unwarranted price changes or price volatility, exists in these regulated markets, and if so to what degree. The question presented is a surprisingly difficult one to answer. All the empirical studies on this question have drawbacks, and none is conclusive. This inconclusivity is not surprising. It is inevitable, given the economic uncertainties that inhere in the data and the complexity of the question. There are many theoretical and empirical assumptions and leaps, that are needed to transform and interpret raw market data into meaningful and persuasive results. There is no decisive statistical method for establishing evidence for or against position limits in the commodity.

Those studies that use Granger causality methodology tend to conclude that there is no evidence of excessive speculation or its consequences on price returns and price volatility, and many industry commenters opposed to position limits used this methodology. But that methodology is peculiarly sensitive to model design choices, and this review has highlighted the modelling decisions that may have affected the ultimate conclusions of these studies. Moreover, there are countervailing Granger studies showing a link between large speculative positions and price volatility. And studies such as Cheng, Kirilenko, and Xiong, *Convective Risk Flows in Commodity Futures Markets* (working paper 2012), indicate that some Granger studies may mask the impact of speculation in times of financial stress.

Those studies that use comovement and cointegration methods tend to conclude there is evidence of deleterious effects of ''excessive speculation.'' Yet comovement tests for correlation, not causation, and a correlation between large financial trading in the commodity markets and price changes and volatility could be driven by a common causal agent such as macroeconomic factors.

Those studies that use models of fundamental supply and demand reach a whole host of divergent opinions on the subject, each opinion only as strong as the many modelling choices.

In this way, the economic literature is inconclusive. Even clearly written, well-respected papers often contain nuances. It is telling that Hamilton, *Causes and Consequences of the Oil Shock of 2007–2008,* Brookings Paper on Economic Activity (2009), has been cited by both proponents and opponents of position limits.

What can be said with certainty is summarized in the Commission's Notice of Proposed Rulemaking: That large speculative positions and outsized market power pose risks to a well-functioning marketplace. These risks may very well differ depending on commodity market structure, but can in some markets cause real-world price impacts through a higher risk premium as a component of total price. There are also economic studies indicating some correlation between increased speculation and price volatility in times of financial stress, but this correlation does not imply causation.

Comment letters on either side declaring that the matter is settled in their favor among respectable economists are simply incorrect. The best economists on both sides of the debate concede that there is a legitimate debate. This analysis concludes that the academic debate amongst economists about the effects of outsized market positions has reputable and legitimate standard-bearers for opposing positions.

*B. Appendix B—List of Comment Letters Cited in this Rulemaking*

1. Agri-Mark, Inc.; (CL–Agri–Mark–59609, 2/10/2014)
2. Airlines for America (''A4A''); (CL–A4A–59714, 2/10/2014); (CL–A4A–59686, 2/10/2014)
3. Alternative Investment Management Association (''AIMA''); (CL–AIMA–59618, 2/10/2014); (CL–AIMA–59619, 2/10/2014)
4. American Bakers Association (''Bakers''); (CL–Bakers–59691, 2/10/2014)
5. American Benefits Council (''ABC''); (CL–ABC–59670, 2/10/2014)
6. American Cotton Shippers Association (''ACSA''); (CL–ASCA–59667, 2/10/2014)
7. American Farm Bureau Federation (''AFBF''); (CL–AFBF–59730, 2/10/2014)
8. American Feed Industry Association (''AFIA''); (CL–AFIA–60955, 7/13/2016)
9. American Gas Association (''AGA''), (CL–AGA–59632, 2/10/2014); (CL–AGA–

[1733] The undated CME study on conditional spot-month limits is the only empirical work submitted by CME in is opposition to the position limits rulemaking. It has been proven wrong. The Commission has previously explained that CME made technical data errors in doing its analysis. Position Limits for Futures and Swaps, 76 FR 71626, 71635 nn. 100–101 (Nov. 18, 2011). The European Commission publication in CME's first set of submissions, *Tackling the Challenges in Commodity Markets and Raw Materials,* European Commission (2011) (2.2.2011), is simply a discussion of policy initiatives. It concedes that it is difficult to know which way causation forms between financial and physical markets and states that ''the debate . . . is still open'' on whether financial inflows have affected prices. *Id.* at 2, 7.

59633, 2/10/2014); (CL–AGA–60382, 3/30/2015); (CL–AGA–60943, 7/13/2016)
10. American Petroleum Institute (''API''); (CL–API–59694, 2/10/2014); (CL–API–59944, 8/4/2014); (CL–API–60939, 7/13/2016)
11. American Public Gas Association (''APGA''); (CL–APGA–59722, 2/10/2014)
12. American Sugar Refining, Inc.; (CL–ASR–59668, 2/10/2014); (CL–ASR–60933, 7/13/2016)
13. Americans for Financial Reform (''AFR''); (CL–AFR–59711, 2/10/2014); (CL–AFR–59685, 2/10/2014); (CL–AFR–60953, 7/13/2016)
14. Archer Daniels Midland Company (''ADM''); (CL–ADM–59640, 2/10/2014); (CL–ADM–60300, 1/22/2015); (CL–ADM–60934, 7/13/2016)
15. Armajaro Asset Management; (CL–Armajaro–59729, 2/10/2014)
16. Atmos Energy Holdings, Inc. (''Atmos''); (CL–Atmos–59705, 2/10/2014)
17. Better Markets, Inc.; (CL–Better Markets–59715, 2/10/2014); (CL–Better Markets–59716, 2/10/2014); (CL–Better Markets–60325, 1/22/2015); (CL–Better Markets–60401, 3/30/2015); (CL–Better Markets–60928, 7/13/2016)
18. BG Energy Merchants, LLC (''BG Group''); (CL–BG Group–59656, 2/10/2014); (CL–BG Group–59937, 8/4/2014); (CL–BG Group–60383, 3/30/2015)
19. Cactus Feeders, Inc., et al.; (CL–Cactus–59660, 2/10/2014)
20. Calpine Corporation; (CL–Calpine–59663, 2/10/2014)
21. Cargill, Incorporated; (CL–Cargill–59638, 2/10/2014)
22. Castleton Commodities International LLC (''CCI''); (CL–CCI–60935, 7/13/2016)
23. Center for Capital Markets Competitiveness, U.S. Chamber of Commerce (''Chamber''); (CL–Chamber–59684, 2/10/2014); (CL–Chamber–59721, 2/10/2014)
24. Chairman, U.S. Senate Permanent Subcommittee on Investigations of the Committee on Homeland Security and Governmental Affairs; (CL–Sen. Levin–59637, 2/10/2014)
25. Citadel LLC; (CL–Citadel–59717, 2/10/2014); (CL–Citadel–59933, 8/1/2014)
26. CME Group Inc. (''CME''); (CL–CME–59719, 2/10/2014); (CL–CME–59718, 2/10/2014); (CL–CME–59970, 8/4/2014); (CL–CME–59971, 8/4/2014); (CL–CME–60307, 1/22/2015); (CL–CME–60406, 3/30/2015); (CL–CME–60926, 7/13/2016)
27. Coalition of Physical Energy Companies (''COPE''); (CL–COPE–59662, 2/10/2014); (CL–COPE–59653, 2/10/2014); (CL–COPE–59950, 8/4/2014); (CL–COPE–60388, 3/30/2015); (CL–COPE–60932, 7/13/2016)
28. Commercial Energy Working Group; (CL–Working Group–59647, 2/10/2014)
29. Commodities Working Group of GFMA (''GFMA''); (CL–GFMA–60314, 1/22/2015)
30. Commodity Markets Council (''CMC''); (CL–CMC–59634, 2/10/2014); (CL–CMC–59925, 7/25/2014); (CL–CMC–60318, 1/22/2015); (CL–CMC–60391, 3/30/2015); (CL–CMC–60950, 7/13/2016)
31. Commodity Markets Oversight Coalition (''CMOC''); (CL–CMOC–59720, 2/10/2014); (CL–CMOC–60324, 1/22/2015); (CL–CMOC–60400, 3/30/2015)
32. Committee on Capital Markets Regulation (''CCMR''); (CL–CCMR–59623, 2/10/2014)
33. Copperwood Asset Management LP (''CAM''); (CL–CAM–60097, 12/22/2014)
34. Cota, Sean; (CL–Cota–59706, 2/10/2014); (CL–Cota–60322, 1/22/2015)
35. CSC Sugar, LLC (''CSC''); (CL–CSC–59676, 2/10/2014); (CL–CSC–59677, 2/10/2014)
36. Dairy Farmers of America (''DFA''); (CL–DFA–59621, 2/10/2014); (CL–DFA–59948, 8/4/2014); (CL–DFA–60309, 1/22/2015); (CL–DFA–60927, 7/13/2016)
37. Darigold; (CL–Darigold–59651, 2/10/2014)
38. Davis Wright Tremaine LLP on behalf of Dairy America, Inc.; (CL–Dairy America–59683, 2/10/2014)
39. DB Commodity Services LLC (''DBCS''); (CL–DBCS–59569, 2/6/2014)
40. Duke Energy Utilities; (CL–DEU–59627, 2/10/2014)
41. Ecom Agro Industrial, Inc.; (CL–Ecom–60308, 1/22/2015)
42. EDF Trading North America, LLC (''EDF''); (CL–EDF–59961, 8/4/2014); (CL–EDF–60398, 3/30/2015); (CL–EDF–60944, 7/13/2016)
43. Edison Electric Institute (''EEI''); (CL–EEI–59945, 8/4/2014); (CL–EEI–Sup–60386, 3/30/2015)
44. Electric Power Supply Association (''EPSA''); (CL–EPSA–55953, 8/4/2014); (CL–EPSA–59999, 11/12/2014); (CL–EPSA–60381, 3/30/2015)
45. EEI and EPSA, jointly (''EEI–EPSA''); (CL–EEI–EPSA–59602, 2/7/2014); (CL–EEI–EPSA–60925, 7/13/2016)
46. Energy Transfer Partners, L.P. (''ETP''); (CL–ET–59958, 8/4/2014); (CL–ETP–60915, 7/12/2016)
47. FC Stone LLC; (CL–FCS–59675, 2/10/2014)
48. Fonterra Co-operative Group Limited (''Fonterra''); (CL–Fonterra–59608, 2/9/2014)
49. Futures Industry Association (''FIA''), (CL–FIA–59595, 2/7/2014); (CL–FIA–59566, 2/6/2014); (CL–FIA–59931, 7/31/2014); (CL–FIA–60303, 1/22/2015); (CL–FIA–60392, 3/30/2015); (CL–FIA–60937, 7/13/2016)
50. Grain Service Corporation (''GSC''); (CL–GSC–59703, 2/10/2014)
51. HP Hood LLC (''Hood''), (CL–Hood–59582, 2/7/2014)
52. ICE Futures U.S., Inc.; (CL–ICE–59645, 2/10/2014); (CL–ICE–59649, 2/10/2014); (CL–ICE–59938, 8/4/2014); (CL–ICE–60310, 1/22/2015); (CL–ICE–60311, 1/22/2015); (CL–ICE–60378, 3/30/2015)
53. Industrial Energy Consumers of America; (CL–IECA–59671, 2/10/2014); (CL–IECA–59713, 2/10/2014); (CL–IECA–59964, 8/4/2014); (CL–IECA–60389, 3/30/2015)
54. Innovation Center for US Dairy; (CL–US Dairy–59952, 8/4/2014)
55. Institute for Agriculture and Trade Policy (''IATP''); (CL–IATP–59701, 2/10/2014); (CL–IATP–59704, 2/10/2014); (CL–IATP–60394, 3/30/2015); (CL–IATP–60951, 7/13/2016)
56. IATP and AFR, jointly; (CL–IATP–60323, 1/22/2015)
57. Intercontinental Exchange, Inc. (''ICE''); (CL–ICE–59669, 2/10/2014); (CL–ICE–59962, 8/4/2014); (CL–ICE–59966, 8/4/2014); (CL–ICE–60387, 3/30/2015); (CL–ICE–60929, 7/13/2016)
58. International Dairy Foods Association (''IDFA''); (CL–IDFA–59771, 2/10/2014)
59. International Energy Credit Association; (CL–IECAssn–9679, 2/10/2014); (CL–IECAssn–59957, 8/4/2014); (CL–IECAssn–60395, 3/30/2015); (CL–IECAssn–60949, 7/13/2016)
60. International Swaps and Derivatives Association, Inc. (''ISDA''); (CL–ISDA–60370, 3/26/2015); (CL–ISDA–60931, 7/13/2016)
61. Investment Company Institute (''ICI''); (CL–ICI–59614, 2/10/2014)
62. ISDA and SIFMA, jointly; (CL–ISDA/SIFMA–59611, 2/10/2014); (CL–ISDA/SIFMA–59917, 7/7/2014)
63. Just Energy Group Inc.; (CL–Just–59692, 2/10/2014)
64. Leprino Foods Company; (CL–Leprino–59707, 2/10/2014)
65. Louis Dreyfus Commodities LLC; (CL–LDC–59643, 2/10/2014)
66. Managed Funds Association (''MFA''); (CL–MFA–59600, 2/7/2014); (CL–MFA–59606, 2/9/2014); (CL–MFA–60385, 3/30/2015)
67. MidAmerican Energy Holdings Company; (CL–MidAmerican–59585, 2/7/2014)
68. Minneapolis Grain Exchange, Inc. (''MGEX''); (CL–MGEX–59610, 2/10/2014); (CL–MGEX–59932, 8/1/2014); (CL–MGEX–60301, 1/22/2015); (CL–MGEX–60380, 3/30/2015); (CL–MGEX–60936, 7/13/2016); (CL–MGEX–60938, 7/13/2016)
69. Morgan Stanley; (CL–MSCGI–59708, 2/10/2014)
70. National Association of Wheat Growers; (CL–NAWG–59687, 2/10/2014)
71. National Cattlemen's Beef Association (''NCBA''); (CL–NCBA–59624, 2/10/2014)
72. National Corn Growers Association & American Soybeans Association, jointly; (CL–NCGA–ASA–60917, 7/12/2016)
73. National Corn Growers Association & Natural Gas Supply Association, jointly; (CL–NCGA–NGSA–60919, 7/13/2016)
74. National Cotton Council of America, American Cotton Shippers Association, and Amcot, jointly; (CL–NCC–ACSA–60972, 7/18/2016)
75. National Council of Farmer Cooperatives; (CL–NCFC–59613, 2/10/2014); (CL–NCFC–59942, 8/4/2014); (CL–NCFC–60930, 7/13/2016)
76. National Energy Marketers Association; (CL–NEM–59586, 2/7/2014); (CL–NEM–59620, 2/10/2014)
77. National Grain and Feed Association; (CL–NGFA–59681, 2/10/2014); (CL–NGFA–59956, 8/4/2014); (CL–NGFA–60267, 1/17/2015); (CL–NGFA–60312, 1/22/2015); (CL–NGFA–60941, 7/13/2016)
78. National Milk Producers Federation; (CL–NMPF–59652, 2/10/2014); (CL–NMPF–60956, 7/13/2016)

79. National Rural Electric Cooperative Association, American Public Power Association, and the Large Public Power Council, jointly (the ''NFP Electric Associations''); (CL–NFP–59690, 2/10/2014); (CL–NFP–59934, 8/1/2014); (CL–NFP–60393, 3/30/2015); (CL–NFP–60942, 7/13/2016)
80. Natural Gas Supply Association; (CL–NGSA–59673, 2/10/2014); (CL–NGSA–59674, 2/10/2014); (CL–NGSA–59900, 6/26/2014); (CL–NGSA–59941, 8/4/2014); (CL–NGSA–60379, 3/30/2015)
81. Nebraska Cattlemen Inc.; (CL–NC–59696, 2/10/2014)
82. New York State Department of Agriculture & Markets; (CL–NYS Agriculture–59657, 2/10/2014)
83. Nodal Exchange, LLC; (CL–Nodal–59695, 2/10/2014); (CL–Nodal–60948, 7/13/2016)
84. NRG Energy, Inc.; (CL–NRG–60434, 1/20/2015)
85. Occupy the SEC (''OSEC''); (CL–OSEC–59972, 8/7/2014)
86. Olam International Limited; (CL–Olam–59658, 2/10/2014); (CL–Olam–59946, 8/4/2014)
87. Pedestal Commodity Group, LLC; (CL–Pedestal–59630, 2/10/2014)
88. Petroleum Marketers Association of America and the New England Fuel Institute; (CL–PMAA–NEFI–60952, 7/13/2016)
89. Plains All American Pipeline, L.P.; (CL–PAAP–59664, 2/10/2014); (CL–PAAP–59951, 8/4/2014)
90. Private Equity Growth Capital Council (''PEGCC''); (CL–PEGCC–59650, 2/10/2014); (CL–PEGCC–59913, 7/3/2014); (CL–PEGCC–59987, 10/24/2014)
91. Public Citizen, Inc.; (CL–Public Citizen–59648, 2/10/2014); (CL–Public Citizen–60390, 3/30/2015); (CL–Public Citizen–60313, 1/22/2015); (CL–Public Citizen–60940, 7/13/2016)
92. Rice Dairy LLC; (CL–Rice Dairy–59601, 2/7/2014); (CL–Rice Dairy–59960, 8/4/2014)
93. RightingFinance; (CL–RF–60372, 3/28/2015)
94. Risk Management Work Group, Globalization Operating Committee, Innovation Center for US Dairy; (CL–US Dairy–59597, 2/7/2014)
95. Rutkowski, Robert; (CL–Rutkowski–60961, 7/14/2016); (CL–Rutkowski-60962, 7/14/2016)
96. Sempra Energy; (CL–SEMP–59926, 7/25/2014); (CL–SEMP–60384, 3/30/2015)
97. SIFMA AMG (''SIFMA''); (CL–AMG–59709, 2/10/2014); (CL–AMG–59710, 2/10/2014); (CL–AMG–59935, 8/1/2014); (CL–AMG–60946, 7/13/2016)
98. Southern Company Services, Inc.; (CL–SCS–60399, 3/30/2015)
99. Sutherland Asbill & Brennan LLP on behalf of The Commercial Energy Working Group; (CL–Working Group–59693, 2/10/2014); (CL–Working Group–59955, 8/4/2014); (CL–Working Group–59959, 8/4/2014); (CL–Working Group–60396, 3/30/2015); (CL–Working Group–60947, 7/13/2016)
100. T.C. Jacoby & Company, Inc.; (CL–Jacoby–59622, 2/10/2014)
101. Texas Cattle Feeders Association (''TCFA''); (CL–TCFA–59680, 2/10/2014); (CL–TCFA–59723, 2/10/2014)
102. The Andersons, Inc.; (CL–Andersons–60256, 1/15/2015)
103. The McCully Group LLC; (CL–McCully–59592, 2/7/2014)
104. Thornton, Pamela; (CL–Thornton–59702, 2/10/2014)
105. Traditum Group LLC; (CL–Traditum–59655, 2/10/2014)
106. Tri-State Coalition for Responsible Investment, et al.; (CL–Tri-State–59682, 2/10/2014)
107. United States Commodity Funds LLC (''USCF''); (CL–USCF–59644, 2/10/2014)
108. Vectra Capital LLC; (CL–Vectra–60369, 3/26/2015)
109. Wholesale Markets Brokers Association, Americas (''WMBA''); (CL–WMBA–60945, 7/13/2016)
110. World Economy, Ecology & Development (''WEED''); (CL–WEED–59628, 2/10/2014)
111. World Gold Council (''WGC''); (CL–WGC–59558, 2/6/2014)

**List of Subjects**

*17 CFR Part 1*

Agricultural commodity, Agriculture, Brokers, Committees, Commodity futures, Conflicts of interest, Consumer protection, Definitions, Designated contract markets, Directors, Major swap participants, Minimum financial requirements for intermediaries, Reporting and recordkeeping requirements, Swap dealers, Swaps.

*17 CFR Part 15*

Brokers, Commodity futures, Reporting and recordkeeping requirements, Swaps.

*17 CFR Part 17*

Brokers, Commodity futures, Reporting and recordkeeping requirements, Swaps.

*17 CFR Part 19*

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

*17 CFR Part 37*

Registered entities, Registration application, Reporting and recordkeeping requirements, Swaps, Swap execution facilities.

*17 CFR Part 38*

Block transaction, Commodity futures, Designated contract markets, Reporting and recordkeeping requirements, Transactions off the centralized market.

*17 CFR Part 140*

Authority delegations (Government agencies), Conflict of interests, Organizations and functions (Government agencies).

*17 CFR Part 150*

Bona fide hedging, Commodity futures, Cotton, Grains, Position limits, Referenced Contracts, Swaps.

*17 CFR Part 151*

Bona fide hedging, Commodity futures, Cotton, Grains, Position limits, Referenced Contracts, Swaps.

For the reasons stated in the preamble, the Commodity Futures Trading Commission proposes to amend 17 CFR chapter I as follows:

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

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

**Authority:** 7 U.S.C. 1a, 2, 5, 6, 6a, 6b, 6c, 6d, 6e, 6f, 6g, 6h, 6i, 6k, 6l, 6m, 6n, 6o, 6p, 6r, 6s, 7, 7a–1, 7a–2, 7b, 7b–3, 8, 9, 10a, 12, 12a, 12c, 13a, 13a–1, 16, 16a, 19, 21, 23, and 24 (2012).

### § 1.3(z) [Removed and Reserved]

■ 2. Remove and reserve § 1.3(z).

### § 1.47 [Removed and Reserved]

■ 3. Remove and reserve § 1.47.

### § 1.48 [Removed and Reserved]

■ 4. Remove and reserve § 1.48.

## PART 15—REPORTS—GENERAL PROVISIONS

■ 5. The authority citation for part 15 continues 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 VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111–203, 124 Stat. 1376 (2010).

■ 6. In § 15.00, revise paragraph (p) to read as follows:

### § 15.00 Definitions of terms used in parts 15 through 19, and 21 of this chapter.

* * * * *

(p) *Reportable position* means:

(1) For reports specified in parts 17 and 18 and in § 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 futures of any commodity on any one reporting market, excluding futures 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 position in commodity derivative contracts, as defined in § 150.1 of this chapter, that exceeds a position limit in § 150.2 of this chapter for the particular commodity.

* * * * *

■ 7. In § 15.01, revise paragraph (d) to read as follows:

**§ 15.01 Persons required to report.**

* * * * *

(d) Persons, as specified in part 19 of this chapter, who either:

(1) Hold or control commodity derivative contracts (as defined in § 150.1 of this chapter) that exceed a position limit in § 150.2 of this chapter for the commodities enumerated in that section; or

(2) Are merchants or dealers of cotton holding or controlling positions for future delivery in cotton that equal or exceed the amount set forth in § 15.03.

* * * * *

■ 8. Revise § 15.02 to read as follows:

**§ 15.02 Reporting forms.**

Forms on which to report may be obtained from any office of the Commission or via the Internet (*http://www.cftc.gov*). Forms to be used for the filing of reports follow, and persons required to file these forms may be determined by referring to the rule listed in the column opposite the form number.

| Form No. | Title | Rule |
|---|---|---|
| 40 | Statement of Reporting Trader | 18.04 |
| 71 | Identification of Omnibus Accounts and Sub-accounts | 17.01 |
| 101 | Positions of Special Accounts | 17.00 |
| 102 | Identification of Special Accounts, Volume Threshold Accounts, and Consolidated Accounts | 17.01 |
| 204 | Statement of Cash Positions of Hedgers | 19.00 |
| 304 | Statement of Cash Positions for Unfixed-Price Cotton "On Call" | 19.00 |
| 504 | Statement of Cash Positions for Conditional Spot Month Exemptions | 19.00 |
| 604 | Statement of Pass-Through Swap Exemptions | 19.00 |

(Approved by the Office of Management and Budget under control numbers 3038–0007, 3038–0009, and 3038–0103.)

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

■ 9. The authority citation for part 17 continues to read as follows:

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

■ 10. In § 17.00, revise paragraph (b) to read as follows:

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

* * * * *

(b) *Interest in or control of several accounts.* Except as otherwise instructed by the Commission or its designee and as specifically provided in § 150.4 of this chapter, if any person holds or has a financial interest in or controls more than one account, all such accounts shall be considered by the futures commission merchant, clearing member or foreign broker as a single account for the purpose of determining special account status and for reporting purposes.

* * * * *

■ 11. In § 17.03, revise paragraph (h) to read as follows:

**§ 17.03 Delegation of authority to the Director of the Office of Data and Technology or the Director of the Division of Market Oversight.**

* * * * *

(h) Pursuant to § 17.00(b), and as specifically provided in § 150.4 of this chapter, the authority shall be designated to the Director of the Office of Data and Technology to instruct a futures commission merchant, clearing member or foreign broker to consider otherwise than as a single account for the purpose of determining special account status and for reporting purposes all accounts one person holds or controls, or in which the person has a financial interest.

* * * * *

■ 12. Revise part 19 to read as follows:

## PART 19—REPORTS BY PERSONS HOLDING POSITIONS EXEMPT FROM POSITION LIMITS AND BY MERCHANTS AND DEALERS IN COTTON

Sec.


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

**§ 19.00 General provisions.**

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

(1) *Persons filing for exemption to speculative position limits.* All persons holding or controlling positions in commodity derivative contracts, as defined in § 150.1 of this chapter, in excess of any speculative position limit provided under § 150.2 of this chapter and for any part of which a person relies on an exemption to speculative position limits under § 150.3 of this chapter as follows:

(i) *Conditional spot month limit exemption.* A conditional spot month limit exemption under § 150.3(c) of this chapter for any commodity specially designated by the Commission under § 19.03 for reporting;

(ii) *Pass-through swap exemption.* A pass-through swap exemption under § 150.3(a)(1)(i) of this chapter and as defined in paragraph (2)(ii)(B) of the definition of *bona fide hedging position* in § 150.1 of this chapter, reporting separately for:

(A) *Non-referenced-contract swap offset.* A swap that is not a referenced contract, as that term is defined in § 150.1 of this chapter, and which is executed opposite a counterparty for which the swap would qualify as a bona fide hedging position and for which the risk is offset with a referenced contract; and

(B) *Spot-month swap offset.* A cash-settled swap, regardless of whether it is a referenced contract, executed opposite a counterparty for which the swap would qualify as a bona fide hedging position and for which the risk is offset with a physical-delivery referenced contract in its spot month;

(iii) *Other exemption.* Any other exemption from speculative position limits under § 150.3 of this chapter, including for a bona fide hedging position as defined in § 150.1 of this chapter or any exemption granted under § 150.3(b) or (d) of this chapter; or

(iv) *Anticipatory exemption.* An anticipatory exemption under § 150.7 of this chapter.

(2) *Persons filing cotton on call reports.* Merchants and dealers of cotton holding or controlling positions for futures delivery in cotton that are reportable pursuant to § 15.00(p)(1)(i) of this chapter; or

(3) *Persons responding to a special call.* All persons exceeding speculative position limits under § 150.2 of this chapter or all persons holding or controlling positions for future delivery that are reportable pursuant to § 15.00(p)(1) of this chapter who have received a special call for series '04 reports from the Commission or its designee. Persons subject to a special call shall file CFTC Form 204, 304, 504, or 604 as instructed in the special call. 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.

(b) *Manner of reporting.* The manner of reporting the information required in § 19.01 is subject to the following:

(1) *Excluding certain source commodities, products or byproducts of the cash commodity hedged.* If the regular business practice of the reporting person is to exclude certain source commodities, products or byproducts in determining his cash positions for bona fide hedging positions (as defined in § 150.1 of this chapter), the same shall be excluded in the report, provided that the amount of the source commodity being excluded is de minimis, impractical to account for, and/or on the opposite side of the market from the market participant's hedging position. Such persons shall furnish to the Commission or its designee upon request detailed information concerning the kind and quantity of source commodity, product or byproduct so excluded. *Provided however,* when reporting for the cash commodity of soybeans, soybean oil, or soybean meal, the reporting person shall show the cash positions of soybeans, soybean oil and soybean meal.

(2) *Cross hedges.* Cash positions that represent a commodity, or products or byproducts of a commodity, that is different from the commodity underlying a commodity derivative contract that is used for hedging, shall be shown both in terms of the equivalent amount of the commodity underlying the commodity derivative contract used for hedging and in terms of the actual cash commodity as provided for on the appropriate series '04 form.

(3) *Standards and conversion factors.* In computing their cash position, every person shall use such standards and conversion factors that are usual in the particular trade or that otherwise reflect the value-fluctuation-equivalents of the cash position in terms of the commodity underlying the commodity derivative contract used for hedging. Such person shall furnish to the Commission upon request detailed information concerning the basis for and derivation of such conversion factors, including:

(i) The hedge ratio used to convert the actual cash commodity to the equivalent amount of the commodity underlying the commodity derivative contract used for hedging; and

(ii) An explanation of the methodology used for determining the hedge ratio.

**§ 19.01 Reports on stocks and fixed price purchases and sales.**

(a) *Information required*—(1) *Conditional spot month limit exemption.* Persons required to file '04 reports under § 19.00(a)(1)(i) shall file CFTC Form 504 showing the composition of the cash position of each commodity underlying a referenced contract that is held or controlled including:

(i) The as of date;

(ii) The quantity of stocks owned of such commodity that either:

(A) Is in a position to be delivered on the physical-delivery core referenced futures contract; or

(B) Underlies the cash-settled core referenced futures contract;

(iii) The quantity of fixed-price purchase commitments open providing for receipt of such cash commodity in:

(A) The delivery period for the physical-delivery core referenced futures contract; or

(B) The time period for cash-settlement price determination for the cash-settled core referenced futures contract;

(iv) The quantity of unfixed-price sale commitments open providing for delivery of such cash commodity in:

(A) The delivery period for the physical-delivery core referenced futures contract; or

(B) The time period for cash-settlement price determination for the cash-settled core referenced futures contract;

(v) The quantity of unfixed-price purchase commitments open providing for receipt of such cash commodity in:

(A) The delivery period for the physical-delivery core referenced futures contract; or

(B) The time period for cash-settlement price determination for the cash-settled core referenced futures contract; and

(vi) The quantity of fixed-price sale commitments open providing for delivery of such cash commodity in:

(A) The delivery period for the physical-delivery core referenced futures contract; or

(B) The time period for cash-settlement price determination for the cash-settled core referenced futures contract.

(2) *Pass-through swap exemption.* Persons required to file '04 reports under § 19.00(a)(1)(ii) shall file CFTC Form 604:

(i) *Non-referenced-contract swap offset.* For each swap that is not a referenced contract and which is executed opposite a counterparty for which the transaction would qualify as a bona fide hedging position and for which the risk is offset with a referenced contract, showing:

(A) The underlying commodity or commodity reference price;

(B) Any applicable clearing identifiers;

(C) The notional quantity;

(D) The gross long or short position in terms of futures-equivalents in the core referenced futures contract; and

(E) The gross long or short positions in the referenced contract for the offsetting risk position; and

(ii) *Spot-month swap offset.* For each cash-settled swap executed opposite a counterparty for which the transaction would qualify as a bona fide hedging position and for which the risk is offset with a physical-delivery referenced contract held into a spot month, showing for such cash-settled swap that is not a referenced contract the information required under paragraph (a)(2)(i) of this section and for such cash-settled swap that is a referenced contract:

(A) The gross long or short position for such cash-settled swap in terms of futures-equivalents in the core referenced futures contract; and

(B) The gross long or short positions in the physical-delivery referenced contract for the offsetting risk position.

(3) *Other exemptions.* Persons required to file '04 reports under § 19.00(a)(1)(iii) shall file CFTC Form 204 reports showing the composition of the cash position of each commodity hedged or underlying a reportable position in units of such commodity and in terms of futures equivalents of the core referenced futures contract, including:

(i) The as of date, the commodity derivative contract held or controlled, and the equivalent core referenced futures contract;

(ii) The quantity of stocks owned of such commodities and their products and byproducts;

(iii) The quantity of fixed-price purchase commitments open in such cash commodities and their products and byproducts;

(iv) The quantity of fixed-price sale commitments open in such cash commodities and their products and byproducts;

(v) The quantity of unfixed-price purchase and sale commitments open in such cash commodities and their products and byproducts, in the case of offsetting unfixed-price cash commodity sales and purchases; and

(vi) For cotton, additional information that includes:

(A) The quantity of equity in cotton held, by merchant, producer or agent, by the Commodity Credit Corporation under the provisions of the Upland Cotton Program of the Agricultural Stabilization and Conservation Service of the U.S. Department of Agriculture;

(B) The quantity of certificated cotton owned; and

(C) The quantity of non-certificated stocks owned.

(4) *Anticipatory exemptions.* Persons required to file '04 reports under § 19.00(a)(1)(iv) shall file CFTC Form 204 monthly on the remaining unsold, unfilled and other anticipated activity for the Specified Period that was reported on such person's most recent initial statement or annual update filed on Form 704, pursuant to § 150.7 (e) of this chapter.

(b) *Time and place of filing reports*—(1) *General.* Except for reports specified in paragraphs (b)(2) or (b)(3) of this section, each report shall be made monthly:

(i) As of the close of business on the last Friday of the month, and

(ii) As specified in paragraph (b)(4) of this section, and not later than 9 a.m. Eastern Time on the third business day following the date of the report.

(2) *Spot month reports.* Persons required to file '04 reports under § 19.00(a)(1)(i) for special commodities as specified by the Commission under § 19.03 or under § 19.00(a)(1)(ii)(B) shall file each report:

(i) As of the close of business for each day the person exceeds the limit during a spot period up to and through the day the person's position first falls below the position limit; and

(ii) As specified in paragraph (b)(4) of this section, and not later than 9 a.m. Eastern Time on the next business day following the date of the report.

(3) *Special calls.* Persons required to file '04 reports in response to special calls made under § 19.00(a)(3) shall file each report as specified in paragraph (b)(4) of this section within one business day of receipt of the special call unless otherwise specified in the call.

(4) *Electronic filing.* CFTC '04 reports must be transmitted using the format, coding structure, and electronic data transmission procedures approved in writing by the Commission.

**§ 19.02 Reports pertaining to cotton on call purchases and sales.**

(a) *Information required.* Persons required to file '04 reports under § 19.00(a)(2) shall file CFTC Form 304 reports showing the quantity of call cotton bought or sold on which the price has not been fixed, together with the respective futures on which the purchase or sale is based. As used herein, call cotton refers to spot cotton bought or sold, or contracted for purchase or sale at a price to be fixed later based upon a specified future.

(b) *Time and place of filing reports.* Each report shall be made weekly as of the close of business on Friday and filed using the procedure under § 19.01(b)(3), not later than 9 a.m. Eastern Time on the third business day following the date of the report.

**§ 19.03 Reports pertaining to special commodities.**

From time to time to facilitate surveillance in certain commodity derivative contracts, the Commission may designate a commodity derivative contract for reporting under § 19.00(a)(1)(i) and will publish such determination in the **Federal Register** and on its Web site. Persons holding or controlling positions in such special commodity derivative contracts must, beginning 30 days after notice is published in the **Federal Register**, comply with the reporting requirements under § 19.00(a)(1)(i) and file Form 504 for conditional spot month limit exemptions.

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

(1) The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director may designate from time to time, the authority in § 19.01 to provide instructions or to determine the format, coding structure, and electronic data transmission procedures for submitting data records and any other information required under this part.

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

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

**§§ 19.05–19.10 [Reserved]**

**Appendix A to Part 19—Forms 204, 304, 504, 604, and 704**

BILLING CODE 6351–01–P

# CFTC FORM 204

## Statement of Cash Positions of Hedgers

**NOTICE:** Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act")[2] and the regulations thereunder,[3] or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both.

**PRIVACY ACT NOTICE**

The Commission's authority for soliciting this information is granted in sections 4a, 4c(b), 4i, 4t and 8a(5) of the CEA and related regulations (see, e.g., 17 CFR § 19.00). The information solicited from entities and individuals engaged in activities covered by the CEA is required to be provided to the CFTC, and failure to comply may result in the imposition of criminal or administrative sanctions (*see*, e.g., 7 U.S.C. §§ 9 and 13a-1, and/or 18 U.S.C. 1001). The information requested is most commonly used in the Commission's market and trade practice surveillance activities to (a) provide information concerning the size and composition of the commodity derivatives markets, (b) permit the Commission to monitor and enforce speculative position limits and (c) enhance the Commission's trade surveillance data. The requested information may be used by the Commission in the conduct of investigations and litigation and, in limited circumstances, may be made public in accordance with provisions of the CEA and other applicable laws. It may also be disclosed to other government agencies and to contract markets to meet responsibilities assigned to them by law. The information will be maintained in, and any additional disclosures will be made in accordance with, the CFTC System of Records Notices, available on www.cftc.gov.

[1] This Appendix includes representations of the proposed reporting forms, which would be submitted in an electronic format published pursuant to the proposed rules, either via the Commission's web portal or via XML-based, secure FTP transmission.

[2] 7 U.S.C. section 1, et seq.

[3] Unless otherwise noted, the rules and regulations referenced in this notice are found in chapter 1 of title 17 of the Code of Federal Regulations; 17 CFR Chapter 1 et seq.

# BACKGROUND & INSTRUCTIONS

Applicable Regulations:

- 17 CFR § 19.00(a)(1)(iii) and (iv) specify who must file Form 204.
- 17 CFR § 19.00(b) specifies the manner of reporting on series '04 reports, including Form 204.
- 17 CFR § 19.01(a)(3) and (4)(ii) specifies the information required on Form 204.
- 17 CFR § 19.01(b)(1) specifies the frequency (**monthly**), the as of report date (close of business on the last Friday of the month), and the time (9 a.m. Eastern Time on the third business day following the date of the report), for filing Form 204.

As appropriate, please follow the instructions below to generate and submit the required report or filing. Relevant regulations are cited in parentheses () for reference. Unless the context requires otherwise, the terms used herein shall have the same meaning as ascribed in parts 15 to 21 of the Commission's regulations.

**Complete Form 204 as follows:**

**The trader identification fields should be completed by all filers.** This updated Form 204 requires traders to identify themselves using their Public Trader Identification Number, in lieu of the CFTC Code Number required on previous versions of the Form 204. This number is provided to traders who have previously filed Forms 40 and 102 with the Commission. Traders may contact the Commission to obtain this number if it is unknown. If a trader has a National Futures Association Identification Number ("NFA ID") and/or a Legal Entity Identifier ("LEI"), he should also identify himself using those numbers. Form 204 requires traders to identify the name of the reporting trader or firm and the contact information (including full name, address, phone number, and email address) for a natural person the Commission may contact regarding the submitted Form 204.

**Section A of Form 204 must be completed by all filers who hold stocks and fixed-price cash positions in the cash commodity. Section A contains the following fields:**

| | |
|---|---|
| Date………………………………… | As-of date for reported position |
| RC or CDC…………………………. | Referenced Contract (§ 150.1) used for hedging or Commodity Derivative Contract (§ 150.1) as required by, e.g., a special call (§ 19.00(a)(3)) |
| CRFC……………………………….. | Corresponding Core Referenced Futures Contract (§ 150.2(d)) |
| Futures Equivalent in CRFC……….. | Quantity of cash commodity hedged, converted to futures equivalents of the CRFC. Short positions should be represented with a minus sign, e.g. 2,000 contract equivalents short = "-2,000" |
| Cash commodity hedged…………… | Cash commodity hedged by the CDC positions, e.g. "crude oil" |
| Units………………………………… | Units of measure for cash commodity being hedged, e.g. "barrels" |
| Stock……………………………….. | Stocks (§ 19.01(a)(3)(ii)) |
| Fixed Price Purchases ……………… | Fixed-price purchase commitments (§ 19.01(a)(3)(iii)) |
| Fixed Price Sales…………………… | Fixed-price sale commitments (§ 19.01(a)(3)(iv)) |
| Remaining Anticipated Activity…… | Remaining Unsold, Unfilled and Other Anticipated Activity for the Specified Period in Form 704 (§ 150.7(g) and § 19.01(a)(4)) |

**Section B of Form 204 must be completed by all filers who hold unfixed-price cash positions in the cash commodity. Section B contains the following fields:**

| | |
|---|---|
| Date………………………………….. | As-of date for reported position |
| RC or CDC…………………………. | Referenced Contract (§ 150.1) used for hedging or Commodity Derivative Contract (§ 150.1) as required by, e.g., a special call (§ 19.00(a)(3)) |
| CRFC……………………………….. | Corresponding Core Referenced Futures Contract (§ 150.2(d)) |

| | |
|---|---|
| Futures Equivalent in CRFC………... | Futures Contract Equivalent in terms of CRFC. Short positions should be represented with a minus sign, e.g. 2,000 contract equivalents short = "-2,000" |
| Cash commodity hedged…………… | Cash commodity hedged by the CDC positions, e.g. "crude oil" |
| Units…………………………………. | Units of measure for cash commodity being hedged, e.g. "barrels" |
| Unfixed-price purchases…………… | Unfixed-price purchases (§ 19.01(a)(3)(v)) |
| Unfixed-price sales………………..... | Unfixed-price sales (§ 19.01(a)(3)(v)) |

**Section C of Form 204 must be completed in addition to Sections A and B of Form 204 by filers who hold cotton stocks. Section C contains the following fields:**

Equity Stocks………………………. Equity stock in hundreds of 500-lb. bales. Traders must report separately equity stocks held in the trader's capacity as a merchant, producer, and/or agent. (§ 19.01(a)(3)(vi))

Certificated Stocks…………………. Certificated stock in hundreds of 500-lb. bales. (§ 19.01(a)(3)(vi))

Non-certificated Stocks…………….. Non-certificated stock in hundreds of 500-lb. bales. (§ 19.01(a)(3)(vi))

**The signature/authorization page must be completed by all filers.** This page must include the name and position of the natural person filing Form 204 as well as the name of the reporting trader represented by that person. The trader certifying this Form 204 on the signature/authorization page should note that filing a report that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both.

***Submitting Form 204:*** Once completed, please submit this form to the Commission pursuant to the instructions on [www.cftc.gov] or as otherwise directed by Commission staff. If submission attempts fail, the reporting trader shall contact the Commission at [techsupport@cftc.gov] for further technical support.

Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

| Public Trader ID No. [provided by CFTC] | OMB No. 3038-0013 |
| --- | --- |

**COMMODITY FUTURES TRADING COMMISSION**
**FORM 204:**
**STATEMENT OF CASH POSITIONS OF HEDGERS**

| Identifying Information | | | |
| --- | --- | --- | --- |
| Identification Codes: | | | |
| NFA ID | | Legal Entity Identifier (LEI) | |
| | | | |
| Name of Reporting Trader or Firm: | | | |
| | | | |
| Name of Person to Contact Regarding This Form: | | | |
| First Name | Middle Name | Last Name | Suffix |
| | | | |
| Contact Information: | | | |
| Address | Phone Number | Email Address | |
| | | | |

NOTICE: Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act") and the regulations thereunder, or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both. Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

A. Cash positions pursuant to the following paragraphs of § 19.01(a)(3)(i), (ii), (iii), (iv), and (4)(ii).

| Date | Referenced Contract (RC) Used for Hedging or Commodity Derivative Contract (CDC) | Core Referenced Futures Contract (CRFC) | Quantity of Cash Commodity Hedged in terms of futures equivalents of the CRFC | Cash Commodity Hedged | Units for Cash Commodity (Specify: e.g. tons, cwt, lbs., bu., bbls., etc.) | Stocks Owned | Fixed-Price Purchases | Fixed-Price Sales | Remaining Unsold, Unfilled and Other Anticipated Activity for the Specified Period in Form 704 |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| | | | | | | | | | |

CFTC Form 204 (XX-XX)
Previous Editions Obsolete

B. Offsetting Unfixed-Price Purchases and Sales pursuant to § 19.01(a)(3)(v).

| Date | Referenced Contract (RC) Used for Hedging or Commodity Derivative Contract (CDC) | Core Referenced Futures Contract (CRFC) | Quantity of Cash Commodity Hedged in terms of futures equivalents of the CRFC | Cash Commodity Hedged | Units for Cash Commodity (Specify: e.g. tons, cwt, lbs., bu., bbls., etc.) | Unfixed-Price Purchases | Unfixed-Price Sales |
|---|---|---|---|---|---|---|---|
| | | | | | | | |

C. Cotton Stocks owned in Section A above pursuant to § 19.01(a)(3)(vi). Report in hundreds of bales (500-lb. bales).

| Equity Stock ('00 bales) as Merchant | Equity Stock ('00 bales) as Producer | Equity Stock ('00 bales) as Agent | Certificated Stocks ('00 bales) | Non-certificated Stocks ('00 bales) |
|---|---|---|---|---|
| | | | | |

CFTC Form 204 (XX-XX)
Previous Editions Obsolete

Please sign/authenticate the Form 204 prior to submitting.

Signature/ Electronic Authentication:

□ By checking this box and submitting this form (or by clicking "submit," "send," or any other analogous transmission command if transmitting electronically), I certify that I am duly authorized by the reporting trader identified below to provide the information and representations submitted on this Form 204, and that to the best of my knowledge the information and representations made herein are true and correct.

Reporting Trader Authorized Representative (Name and Position):

____________________ (Name)

____________________ (Position)

Submitted on behalf of:

____________________ (Reporting Trader Name)

Date of Submission: ____________________

Form 204, Example A- A commercial entity has inventory of 10,000,000 barrels of crude oil, 5,000,000 barrels of crude oil fixed-price sales contracts, and 20,000,000 barrels of crude oil fixed-price purchase contracts. The commercial entity could claim a bona fide hedging exemption for a short position of up to 25,000 contracts in the NYMEX light sweet crude oil futures contract, equivalent to 30,000,000 barrels of crude oil. The commercial entity has other short speculative positions in the futures contract that, absent the bona fide hedging exemption, would cause it to exceed the speculative position limit.

| A. Cash positions pursuant to the following paragraphs of § 19.01 (a) (3) (i), (ii), (iii), (iv), and (4)(ii). | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Date | Referenced Contract (RC) Used for Hedging or Commodity Derivative Contract (CDC) | Core Referenced Futures Contract (CRFC) | Quantity of Cash Commodity Hedged in terms of futures equivalents of the CRFC - = short | Cash Commodity Hedged | Units for Cash Commodity (Specify: e.g. tons, cwt, lbs., bu., bbls., etc.) | Stocks Owned | Fixed-Price Purchases | Fixed-Price Sales | Remaining Unsold, Unfilled and Other Anticipated Activity for the Specified Period in Form 704 |
| 5/6/2017 | CL-NYMEX | CL-NYMEX | 25,000 | Crude oil | Bbls | 10,000,000 | 20,000,000 | 5,000,000 | 0 |
| | | | | | | | | | |

Form 204, Example B- A commercial entity has filed unfilled anticipated requirements in an initial statement on form 704, Section A, in the amount of 120,000,000 MMBtu of natural gas. The current remaining unfilled anticipated requirements are 70,000,000 MMBtu. The person owns stocks of 20,000,000 MMBtu and has entered into fixed-price purchases of 30,000,000 MMBtu. The combined long cash position is long 50,000,000 MMBtu. The total position being hedged, i.e., the remaining unfilled anticipatory requirements of 70,000,000 MMBtu and the long cash position of 50,000,000 MMBtu, equals a long position of 120,000,000 MMBtu in the cash commodity. The commercial entity reports a futures equivalent short position of 10,000 contracts in the CRFC as a hedge, equivalent to short 100,000,000 MMBtu, which is less than the combined long cash position and the remaining unfilled anticipated requirements. Hence, the cash position is partially hedged.

| A. Cash positions pursuant to the following paragraphs of § 19.01 (a) (3) (i), (ii), (iii), (iv), and (4)(ii). | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Date | Referenced Contract (RC) Used for Hedging or Commodity Derivative Contract (CDC) | Core Referenced Futures Contract (CRFC) | Quantity of Cash Commodity Hedged in terms of futures equivalents of the CRFC - = short | Cash Commodity Hedged | Units for Cash Commodity (Specify: e.g. tons, cwt, lbs., bu., bbls., etc.) | Stocks Owned | Fixed-Price Purchases | Fixed-Price Sales | Remaining Unsold, Unfilled and Other Anticipated Activity for the Specified Period in Form 704 |
| 5/6/2017 | HH-NYMEX | NG-NYMEX | 50,000 | Natural gas | MMBtu | 20,000,000 | 30,000,000 | 0 | 70,000,000 |
| | | | | | | | | | |

Form 204, Example C- A commercial entity has entered into offsetting unfixed-price purchase and sale contracts in the amount of 25,000,000 MMBtu of natural gas. The hedging position is a futures equivalent long position of 10,000 contracts and a futures equivalent short position of 10,000 contracts.

| B. Offsetting Unfixed-Price Purchases and Sales pursuant to § 19.01(a)(3) (v). | | | | | | | |
|---|---|---|---|---|---|---|---|
| Date | Referenced Contract (RC) Used for Hedging or Commodity Derivative Contract (CDC) | Core Referenced Futures Contract (CRFC) | Quantity of Cash Commodity Hedged in terms of futures equivalents of the CRFC | Cash Commodity Hedged | Units for Cash Commodity (Specify: e.g. tons, cwt, lbs., bu., bbls., etc.) | Unfixed-Price Purchases | Unfixed-Price Sales |
| 5/6/2017 | HH-NYMEX | NG-NYMEX | 25,000 | Natural Gas | MMBtu | 25,000,000 | |
| | HH-NYMEX | NG-NYMEX | -25,000 | Natural Gas | MMBtu | | 25,000,000 |

Form 204, Example D– A merchant reportable in cotton futures has the following inventory: no equity stock, 100 bales of certificated stock, and 500 bales of non-certificated stock.

| C. Cotton Stocks owned in Section A above pursuant to § 19.01(a)(3)(vi). Report in hundreds of bales (500-lb. bales). | | |
|---|---|---|
| Equity Stock ('00 bales) | Certificated Stocks ('00 bales) | Non-certificated Stocks ('00 bales) |
| 0 | 1 | 5 |

# CFTC FORM 304
# Statement of Cash Positions for Unfixed-Price Cotton "On Call"

**NOTICE:** Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act") [1] and the regulations thereunder,[2] or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 USC 1001) and (b) result in punishment by fine or imprisonment, or both.

## PRIVACY ACT NOTICE

The Commission's authority for soliciting this information is granted in sections 4i and 8 of the CEA and related regulations (see, e.g., 17 CFR § 19.02). The information solicited from entities and individuals engaged in activities covered by the CEA is required to be provided to the CFTC, and failure to comply may result in the imposition of criminal or administrative sanctions (*see*, e.g., 7 U.S.C. §§ 9 and 13a-1, and/or 18 U.S.C. 1001). The information requested is most commonly used in the Commission's market and trade practice surveillance activities to (a) provide information concerning the size and composition of the commodity derivatives markets, (b) permit the Commission to monitor and enforce speculative position limits and (c) enhance the Commission's trade surveillance data. The requested information may be used by the Commission in the conduct of investigations and litigation and, in limited circumstances, may be made public in accordance with provisions of the CEA and other applicable laws. It may also be disclosed to other government agencies and to contract markets to meet responsibilities assigned to them by law. The information will be maintained in, and any additional disclosures will be made in accordance with, the CFTC System of Records Notices, available on www.cftc.gov.

[1] 7 U.S.C. section 1, et seq.

[2] Unless otherwise noted, the rules and regulations referenced in this notice are found in chapter 1 of title 17 of the Code of Federal Regulations; 17 CFR Chapter 1 et seq.

## BACKGROUND & INSTRUCTIONS

Applicable Regulations:

- 17 CFR § 19.00(a)(2) specifies who must file Form 304.
- 17 CFR § 19.00(b) specifies the manner of reporting on series '04 reports, including Form 304.
- 17 CFR § 19.02(a) specifies the information required on Form 304.
- 17 CFR § 19.02(b) specifies the frequency (**weekly**), the as of report date (close of business on Friday), and the time (9 a.m. Eastern Time on the third business day following the date of the report), for filing the Form 304.

As appropriate, please follow the instructions below to generate and submit the required report or filing. Relevant regulations are cited in parentheses () for reference. Unless the context requires otherwise, the terms used herein shall have the same meaning as ascribed in parts 15 to 21 of the Commission's regulations.

**Complete Form 304 as follows:**

**The trader identification fields should be completed by all filers.** This updated Form 304 requires traders to identify themselves using their Public Trader Identification Number, in lieu of the CFTC Code Number required on previous versions of the Form 304. This number is provided to traders who have previously filed Forms 40 and 102 with the Commission. Traders may contact the Commission to obtain this number if it is unknown. If a trader has a National Futures Association Identification Number ("NFA ID") and/or a Legal Entity Identifier ("LEI"), he should also identify himself using those numbers. Form 304 requires traders to identify the name of the reporting trader or firm and the contact information (including full name, address, phone number, and email address) for a natural person the Commission may contact regarding the submitted Form 304.

**Merchants and dealers of cotton must report on Form 304.** Report in hundreds of 500-lb. bales unfixed-price cotton "on-call" pursuant to § 19.02(a). Include under "Call Purchases" stocks on hand for which price has not yet been fixed. For each listed stock, report the delivery month, delivery year, quantity of call purchases, and quantity of call sales.

**The signature/authorization page must be completed by all filers.** This page must include the name and position of the natural person filing Form 304 as well as the name of the reporting trader represented by that person. The trader certifying this Form 304 on the signature/authorization page should note that filing a report that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both.

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***Submitting Form 304:*** Once completed, please submit this form to the Commission pursuant to the instructions on [www.cftc.gov] or as otherwise directed by Commission staff. If submission attempts fail, the reporting trader shall contact the Commission at [techsupport@cftc.gov] for further technical support.

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Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

| Public Trader ID No. [provided by CFTC] | OMB No. 3038-0013 |
|---|---|

**COMMODITY FUTURES TRADING COMMISSION**
**FORM 304**
**STATEMENT OF CASH POSITIONS FOR UNFIXED-PRICE COTTON "ON-CALL"**

| Identifying Information | | | |
|---|---|---|---|
| Identification Codes: | | | |
| NFA ID | Legal Entity Identifier (LEI) | | |
| | | | |
| Name of Reporting Trader or Firm: | | | |
| | | | |
| Name of Person to Contact Regarding This Form: | | | |
| First Name | Middle Name | Last Name | Suffix |
| | | | |
| Contact Information: | | | |
| Address | Phone Number | Email Address | |
| | | | |

NOTICE: Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act") and the regulations thereunder, or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both. Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

Unfixed-price Cotton "on-call" pursuant to § 19.02(a); include under "Call Purchases" stocks on hand for which price has not yet been fixed. Report in hundreds of bales (500-lb. bales).

| Delivery Month | Delivery Year | Call Purchases ('00 bales) | Call Sales ('00 bales) |
|---|---|---|---|
| | | | |

CFTC Form 304 (XX-XX)
Previous Editions Obsolete

Please sign/authenticate the Form 304 prior to submitting.

Signature/ Electronic Authentication:

□ By checking this box and submitting this form (or by clicking "submit," "send," or any other analogous transmission command if transmitting electronically), I certify that I am duly authorized by the reporting trader identified below to provide the information and representations submitted on this Form 304, and that to the best of my knowledge the information and representations made herein are true and correct.

Reporting Trader Authorized Representative (Name and Position):

____________________ (Name)

____________________ (Position)

Submitted on behalf of:

____________________ (Reporting Trader Name)

Date of Submission: ____________________

CFTC Form 304 (XX-XX)
Previous Editions Obsolete

Form 304, Example – July 2017 Call purchases of 200 bales and sales of 1,800 bales; October Call purchases of 6,600 bales and sales of 8,000 bales.

| Unfixed-price Cotton "on-call" pursuant to § 19.02(a); include under "Call Purchases" stocks on hand for which price has not yet been fixed. Report in hundreds of bales (500-lb. bales). | | | |
|---|---|---|---|
| Delivery Month | Delivery Year | Call Purchases ('00 bales) | Call Sales ('00 bales) |
| July | 2017 | 2 | 18 |
| October | 2017 | 66 | 80 |
| | | | |

# CFTC FORM 504

## Statement of Cash Positions for Conditional Spot Month Exemptions

**NOTICE:** Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act")[1] and the regulations thereunder,[2] or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both.

### PRIVACY ACT NOTICE

The Commission's authority for soliciting this information is granted in sections 4a, 4c(b), 4i, 4t and 8a(5) of the CEA and related regulations (see, e.g., 17 CFR § 19.00). The information solicited from entities and individuals engaged in activities covered by the CEA is required to be provided to the CFTC, and failure to comply may result in the imposition of criminal or administrative sanctions (see, e.g., 7 U.S.C. §§ 9 and 13a-1, and/or 18 U.S.C. 1001). The information requested is most commonly used in the Commission's market and trade practice surveillance activities to (a) provide information concerning the size and composition of the commodity derivatives markets, (b) permit the Commission to monitor and enforce speculative position limits and (c) enhance the Commission's trade surveillance data. The requested information may be used by the Commission in the conduct of investigations and litigation and, in limited circumstances, may be made public in accordance with provisions of the CEA and other applicable laws. It may also be disclosed to other government agencies and to contract markets to meet responsibilities assigned to them by law. The information will be maintained in, and any additional disclosures will be made in accordance with, the CFTC System of Records Notices, available on www.cftc.gov.

[1] 7 U.S.C. section 1, et seq.

[2] Unless otherwise noted, the rules and regulations referenced in this notice are found in chapter 1 of title 17 of the Code of Federal Regulations; 17 CFR Chapter 1 et seq.

# BACKGROUND & INSTRUCTIONS

Applicable Regulations:

- 17 CFR § 19.00(a)(1)(i) specifies who must file Form 504.
- 17 CFR § 19.00(b) specifies the manner of reporting on series '04 reports, including Form 504.
- 17 CFR § 19.01(a)(1) specifies the information required on Form 504.
- 17 CFR § 19.01(b)(2) specifies the frequency (**daily during the spot month**), the as of report date (close of business for each day a person exceeds the limit, up to and including the day the person's position first falls below the position limit), and the time (9 a.m. Eastern Time on the next business day following the date of the report) for filing Form 504.

As appropriate, please follow the instructions below to generate and submit the required report or filing. Relevant regulations are cited in parentheses () for reference. Unless the context requires otherwise, the terms used herein shall have the same meaning as ascribed in parts 15 to 21 of the Commission's regulations.

**Complete Form 504 as follows:**

**The trader identification fields should be completed by all filers.** This new Form 504 requires traders to identify themselves using their Public Trader Identification Number. This number is provided to traders who have previously filed Forms 40 and 102 with the Commission. Traders may contact the Commission to obtain this number if it is unknown. If a trader has a National Futures Association Identification Number ("NFA ID") and/or a Legal Entity Identifier ("LEI"), he should also identify himself using those numbers. Form 504 requires traders to identify the name of the reporting trader or firm and the contact information (including full name, address, phone number, and email address) for a natural person the Commission may contact regarding the submitted Form 504.

**Form 504 must be completed for stocks and fixed-price cash positions by all filers claiming a conditional spot month limit exemption. Form 504 contains the following fields:**

| | |
|---|---|
| Date…………………………………….. | As of date for reported position (§ 19.01(a)(1)(i)) |
| CRFC……………………………………. | Core Referenced Futures Contract (§ 150.2(d)) |
| Cash commodity………………………. | Cash commodity identification |
| Units…………………………………….. | Units of measure for cash commodity |
| Stocks………………………………….. | Deliverable stored commodity (§ 19.01(a)(1)(ii)) |
| Fixed-price Purchase…………………. | Fixed-price purchase commitments (§ 19.01(a)(1)(iii)) |
| Fixed-price Sale……………………….. | Fixed-price sale commitments (§ 19.01(a)(1)(iv)) |
| Unfixed-price Purchase………………. | Unfixed-price purchase commitments (§ 19.01(a)(1)(v)) |
| Unfixed-price Sale…………………….. | Unfixed-price sale commitments (§ 19.01(a)(1)(vi)) |

**The signature/authorization page must be completed by all filers.** This page must include the name and position of the natural person filing Form 504 as well as the name of the reporting trader represented by that person. The trader certifying this Form 504 on the signature/authorization page should note that filing a report that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both.

***Submitting Form 504:*** Once completed, please submit this form to the Commission pursuant to the instructions on [www.cftc.gov] or as otherwise directed by Commission staff. If submission attempts fail, the reporting trader shall contact the Commission at [techsupport@cftc.gov] for further technical support.

Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

| Public Trader ID No. [provided by CFTC] | | | | OMB No. 3038-0013 |
|---|---|---|---|---|

**COMMODITY FUTURES TRADING COMMISSION**
**FORM 504**
**STATEMENT OF CASH POSITIONS FOR**
**CONDITIONAL SPOT MONTH LIMIT EXEMPTIONS**

| Identifying Information | | | |
|---|---|---|---|
| Identification Codes: | | | |
| NFA ID | Legal Entity Identifier (LEI) | | |
| | | | |
| Name of Reporting Trader or Firm: | | | |
| | | | |
| Name of Person to Contact Regarding This Form: | | | |
| First Name | Middle Name | Last Name | Suffix |
| | | | |
| Contact Information: | | | |
| Address | Phone Number | Email Address | |
| | | | |

NOTICE: Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act") and the regulations thereunder, or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both. Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

Cash positions pursuant to § 19.01(a)(1).

| Date | Core Reference Futures Contract (CRFC) | Cash Commodity | Units for Cash Commodity (Specify Tons, CWT, Lbs., Bu., Bbls., etc.) | Deliverable Cash Commodity held in Stock or Storage | Fixed-price Cash Purchase Commitment | Fixed-price Cash Sale Commitment | Unfixed-price Cash Purchase Commitment | Unfixed-price Cash Sale Commitment |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | | |

CFTC Form 504 (XX-XX)

Please sign/authenticate the Form 504 prior to submitting.

Signature/ Electronic Authentication:

□ By checking this box and submitting this form (or by clicking “submit,” “send,” or any other analogous transmission command if transmitting electronically), I certify that I am duly authorized by the reporting trader identified below to provide the information and representations submitted on this Form 504, and that to the best of my knowledge the information and representations made herein are true and correct.

Reporting Trader Authorized Representative (Name and Position):

____________________ (Name)

____________________ (Position)

Submitted on behalf of:

____________________ (Reporting Trader Name)

Date of Submission: ____________________

CFTC Form 504 (XX-XX)

Form 504 Example. The spot month for the physical-delivery May 2017 NYMEX Henry Hub Natural Gas (NG) futures contract (the CRFC for natural gas) is from the close of business on April 23 through 5:15 p.m. on the last day of trading, April 26, 2017. A trader holds positions in cash-settled natural gas referenced contracts settling on April 25, 2017, that are in excess of the spot month limit of 2,000 contracts, but that do not exceed 10,000 contracts, on each of April 23, 24, and 25, 2017. That trader does not hold any cash-settled referenced contracts settling on April 26, 2017; however, pursuant to § 19.01(b)(2)(i), a person must also report cash positions through the day the person's position first falls below the position limit. Consistent with claiming the conditional spot month limit exemption, the person holds no position in the May 2017 NYMEX NG contract during the spot month. Each line of the report represents each day of this conditional spot month limit exemption.

The person's purchase and sales commitments have the same delivery period as that of the May 2017 NYMEX NG contract. As of the close of business on April 23, 2017, the person holds: natural gas inventory of 10,000,000 MMBtus; fixed-price purchase contracts of 5,000,000 MMBtus; fixed price sales contracts of 10,000,000 MMBtu; unfixed-price cash purchase contracts of 5,000,000 MMBtu; and unfixed-price cash sales contracts of 5,000,000 MMBtu. The contract prices for each of the unfixed-price sales contracts and the unfixed-price purchase contracts are to become fixed 20 percent per business day on April 24, 25, 26, 27, and 28, 2017. The trader does not execute any cash transactions during the spot month.

| Cash positions pursuant to § 19.01(a)(1). | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Date | Core Reference Futures Contract (CRFC) | Cash Commodity | Units for Cash Commodity (Specify Tons, CWT, Lbs., Bu., Bbls., etc.) | Deliverable Cash Commodity held in Stock or Storage | Fixed-price Cash Purchase Commitment | Fixed-price Cash Sale Commitment | Unfixed-price Cash Purchase Commitment | Unfixed-price Cash Sale Commitment |
| 4/23/2017 | NG-NYMEX | Natural Gas in U.S. | MMBtu | 10,000,000 | 5,000,000 | 10,000,000 | 5,000,000 | 5,000,000 |
| 4/24/2017 | NG -NYMEX | Natural Gas in U.S. | MMBtu | 10,000,000 | 6,000,000 | 11,000,000 | 4,000,000 | 4,000,000 |
| 4/25/2017 | NG-NYMEX | Natural Gas in U.S. | MMBtu | 10,000,000 | 7,000,000 | 12,000,000 | 3,000,000 | 3,000,000 |
| 4/26/2017 | NG-NYMEX | Natural Gas in U.S. | MMBtu | 10,000,000 | 8,000,000 | 13,000,000 | 2,000,000 | 2,000,000 |

# CFTC FORM 604
# Statement of Pass-Through Swap Exemptions

**NOTICE:** Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act")[1] and the regulations thereunder,[2] or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 USC 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both.

**PRIVACY ACT NOTICE**

The Commission's authority for soliciting this information is granted in sections 4a, 4c(b), 4i, 4t and 8a(5) of the CEA and related regulations (*see*, e.g., 17 CFR § 19.00). The information solicited from entities and individuals engaged in activities covered by the CEA is required to be provided to the CFTC, and failure to comply may result in the imposition of criminal or administrative sanctions (see, e.g., 7 U.S.C. §§ 9 and 13a-1, and/or 18 U.S.C. 1001). The information requested is most commonly used in the Commission's market and trade practice surveillance activities to (a) provide information concerning the size and composition of the commodity derivatives markets, (b) permit the Commission to monitor and enforce speculative position limits and (c) enhance the Commission's trade surveillance data. The requested information may be used by the Commission in the conduct of investigations and litigation and, in limited circumstances, may be made public in accordance with provisions of the CEA and other applicable laws. It may also be disclosed to other government agencies and to contract markets to meet responsibilities assigned to them by law. The information will be maintained in, and any additional disclosures will be made in accordance with, the CFTC System of Records Notices, available on www.cftc.gov.

[1] 7 U.S.C. section 1, et seq.

[2] Unless otherwise noted, the rules and regulations referenced in this notice are found in chapter 1 of title 17 of the Code of Federal Regulations; 17 CFR Chapter 1 et seq.

## BACKGROUND & INSTRUCTIONS

Applicable Regulations:

- 17 CFR § 19.00(a)(1)(ii) specifies who must file Form 604.
- 17 CFR § 19.00(b) specifies the manner of reporting on series '04 reports, including Form 604.
- 17 CFR § 19.01(a)(2)(i) and (ii) specify the information required on Form 604.
- For pass-through swaps with non-referenced-contract swap offset: 17 CFR § 19.01(b)(1) specifies the frequency (**monthly**), the as of report date (close of business on the last Friday of the month), and the time (9 a.m. Eastern Time on the third business day following the date of the report) for filing Form 604.
- For pass-through swaps with spot-month swap offset: 17 CFR § 19.01(b)(2) specifies the frequency (**daily during the spot month**), the as of report date (close of business for each day a person exceeds the limit, up to and including the day the person's position first falls below the position limit), and the time (9 a.m. Eastern Time on the next business day following the date of the report) for filing Form 604.

As appropriate, please follow the instructions below to generate and submit the required report or filing. Relevant regulations are cited in parentheses () for reference. Unless the context requires otherwise, the terms used herein shall have the same meaning as ascribed in parts 15 to 21 of the Commission's regulations.

**Complete Form 604 as follows:**

**The trader identification fields should be completed by all filers.** This new Form 604 requires traders to identify themselves using their Public Trader Identification Number. This number is provided to traders who have previously filed Forms 40 and 102 with the Commission. Traders may contact the Commission to obtain this number if it is unknown. If a trader has a National Futures Association Identification Number ("NFA ID") and/or a Legal Entity Identifier ("LEI"), he should also identify himself using those numbers. Form 604 requires traders to identify the name of the reporting trader or firm and the contact information (including full name, address, phone number, and email address) for a natural person the Commission may contact regarding the submitted Form 604.

**Section A of Form 604 must be completed by all filers who hold a non-referenced contract swap offset position. Section A contains the following fields:**

| | |
|---|---|
| Date………………………………………….. | As of date for reported position |
| Underlying Commodity………………….... | Underlying Commodity or Commodity Reference Price that is not a Referenced Contract (§ 19.01(a)(2)(i)(A)) |
| CRFC……………………………………… | Corresponding Core Referenced Futures Contract (§ 150.2(d)) |
| Applicable Clearing Identifier……………. | Clearing Identifier (if swap is cleared) (§ 19.01(a)(2)(i)(B)) |
| Commodity Quantity Unit (CQU)………… | Unit of Measurement for Commodity |
| Notional Quantity…………………………. | Notional Quantity in CQU (§ 19.01(a)(2)(i)(C)) |
| Position in FE in CRFC………………….... | Gross long and short positions in futures equivalents of the CRFC (§ 19.01(a)(2)(i)(D)) |
| Position in RC for offsetting risk…………. | Gross long and short positions in referenced contract offset position (§ 19.01(a)(2)(i)(E)) |

**Section B of Form 604 must be completed by all filers who hold a spot-month swap offset position. Section B contains the following fields:**

| | |
|---|---|
| Date………………………………………….. | As of date for reported position |
| RC or non-RC for swap offset………….... | Underlying Commodity or Commodity Reference Price or Referenced Contract for swap offsetting counterparty's bona fide hedging exemption (§ 19.01(a)(2)(ii)) |
| CRFC……………………………………… | Corresponding Core Referenced Futures Contract (§ 150.2(d)) |
| Applicable Clearing Identifier…………… | Clearing Identifier (if swap is cleared) (§ 19.01(a)(2)(i)(B)) |
| Commodity Quantity Unit (CQU)………. | Unit of Measurement for Commodity |
| Notional Quantity………………………… | Notional Quantity in CQU (§ 19.01(a)(2)(i)(C)) |

| | |
|---|---|
| Position in FE in CRFC…………………. | Gross long and short positions in futures equivalents of the CRFC (§ 19.01(a)(2)(ii)(A)) |
| Position in physical delivery RC for offsetting risk………………………….... | Gross long and short positions in referenced contract offset position (§ 19.01(a)(2)(ii)(B)) |

**The signature/authorization page must be completed by all filers.** This page must include the name and position of the natural person filing Form 604 as well as the name of the reporting trader represented by that person. The trader certifying this Form 604 on the signature/authorization page should note that filing a report that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both.

***Submitting Form 604:*** Once completed, please submit this form to the Commission pursuant to the instructions on [www.cftc.gov] or as otherwise directed by Commission staff. If submission attempts fail, the reporting trader shall contact the Commission at [techsupport@cftc.gov] for further technical support.

Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

| Public Trader ID No. [provided by CFTC] | OMB No. 3038-0013 |
| --- | --- |

**COMMODITY FUTURES TRADING COMMISSION**
**FORM 604**
**STATEMENT OF PASS-THROUGH SWAP EXEMPTIONS**

| Identifying Information | | | |
| --- | --- | --- | --- |
| Identification Codes: | | | |
| NFA ID | Legal Entity Identifier (LEI) | | |
| | | | |
| Name of Reporting Trader or Firm: | | | |
| | | | |
| Name of Person to Contact Regarding This Form: | | | |
| First Name | Middle Name | Last Name | Suffix |
| | | | |
| Contact Information: | | | |
| Address | Phone Number | Email Address | |
| | | | |

NOTICE: Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act") and the regulations thereunder, or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both. Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

A. Non-referenced contract swap offset pursuant to § 19.01(a)(2)(i), reported and submitted **monthly** pursuant to § 19.01(b)(1)

| Date | Underlying Commodity or Commodity Reference Price that is not a Referenced Contract (RC) | Core Referenced Futures contract (CRFC) | Applicable Clearing Identifier | Commodity Quantity Units of Measurement (Specify Tons, Lbs., Bu., Bbls., etc.) | Notional Quantity in CQU | Gross Long Position in Futures Equivalent in the CRFC | Gross Short Position in Futures Equivalent in the CFRC | Gross Long Position in the RC for the Offsetting Risk Position in CQU | Gross Short Position in the RC for the Offsetting Risk Position in CQU |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| | | | | | | | | | |

CFTC Form 604 (XX-XX)

B. Spot-month swap offset pursuant to § 19.01(a)(2)(ii), reported and submitted **daily** pursuant to § 19.01(b)(2) for non-referenced and referenced cash-settled swaps

| Date | Underlying Commodity or Referenced Contract for cash-settled swap offsetting BFH exemption of counterparty | Core Referenced Futures contract (CRFC) | Applicable Clearing Identifier | Commodity Quantity Units of Measurement (Specify Tons, Lbs., Bu., Bbls., etc.) - CQU | Notional Quantity in CQU | Gross Long Position for Cash-settled Swap in Futures Equivalent in the CRFC | Gross Short Position for Cash-settled Swap in Futures Equivalent in the CFRC | Gross Long Position in the Physical-delivery RC for the Offsetting Risk Position in CQU | Gross Short Position in the Physical-delivery RC for the Offsetting Risk Position in CQU |
|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | | |

CFTC Form 604 (XX-XX)

Please sign/authenticate the Form 604 prior to submitting.

Signature/ Electronic Authentication:

□ By checking this box and submitting this form (or by clicking “submit,” “send,” or any other analogous transmission command if transmitting electronically), I certify that I am duly authorized by the reporting trader identified below to provide the information and representations submitted on this Form 604, and that to the best of my knowledge the information and representations made herein are true and correct.

Reporting Trader Authorized Representative (Name and Position):

____________________ (Name)

____________________ (Position)

Submitted on behalf of:

____________________ (Reporting Trader Name)

Date of Submission: ____________________

CFTC Form 604 (XX-XX)

Form 604, Example A. A person offsets a long position in a cash-settled milo swap with a notional size of 5,000,000 bushels, using the CBOT Corn futures contract, as a cross-commodity hedge. The milo swap was a bona fide hedging position for the swap counterparty, and was not cleared. For illustrative purposes, the hedge ratio is assumed to be one-to-one between milo and corn.

| A. Non-referenced contract swap offset pursuant to § 19.01(a)(2)(i), reported and submitted **monthly** pursuant to § 19.01(b)(1) | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Date | Underlying Commodity or Commodity Reference Price that is not a Referenced Contract (RC) | Core Referenced Futures contract (CRFC) | Applicable Clearing Identifier | Commodity Quantity Units of Measurement (Specify Tons, Lbs., Bu., Bbls., etc.) | Notional Quantity in CQU | Gross Long Position in Futures Equivalent in the CRFC | Gross Short Position in Futures Equivalent in the CFRC | Gross Long Position in the RC for the Offsetting Risk Position in CQU | Gross Short Position in the RC for the Offsetting Risk Position in CQU |
| 6/28/2017 | Milo | C-CBOT | NA | Bu | 5,000,000 | 1,000 | 0 | 0 | 5,000,000 |
| | | | | | | | | | |

Form 604, Example B. A person offsets a cash-settled corn swap with a notional size of 5,000,000 bushels, using the CBOT Corn futures contract during the spot month. An exemption for swap offsets is not permitted in the physical-delivery CBOT Corn futures contract in the last five days of trading. For the May 2017 CBOT Corn futures contract, the last day of trading is May 12 (CBOT rules specify the last trading day as the business day preceding the fifteenth calendar day of the contract month). Hence, the spot month swap offset exemption is not available in the May 2017 CBOT Corn futures contract as of the close of business on May 5, 2017. At that time, the trader must comply with the 600 contract spot month limit, equivalent to 3,000,000 bushels of corn, absent another exemption. Each line represents each day's report for this swap offset position. The spot month for the CBOT Corn futures contract begins at the close of trading two business days prior to the first trading day of the delivery month; hence, April 27, 2017, is the start of the spot month for the May 2017 CBOT Corn futures contract. The corn swap was a bona fide hedging position for the swap counterparty, and was not cleared.

| B. Spot-month swap offset pursuant to § 19.01(a)(2)(ii). reported and submitted **daily** pursuant to § 19.01(b)(2) for non-referenced and referenced cash-settled swaps | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Date | Underlying Commodity or Referenced Contract for cash-settled swap offsetting BFH exemption of counterparty | Core Referenced Futures contract (CRFC) | Applicable Clearing Identifier | Commodity Quantity Units of Measurement (Specify Tons, Lbs., Bu., Bbls., etc.) - CQU | Notional Quantity in CQU | Gross Long Position for Cash-settled Swap in Futures Equivalent in the CRFC | Gross Short Position for Cash-settled Swap in Futures Equivalent in the CFRC | Gross Long Position in the Physical-delivery RC for the Offsetting Risk Position in CQU | Gross Short Position in the Physical-delivery RC for the Offsetting Risk Position in CQU |
| 4/27/2017 | Corn swap | C-CBOT | NA | Bu | 5,000,000 | 1,000 | 0 | 0 | 5,000,000 |
| 4/28/2017 | Corn swap | C-CBOT | NA | Bu | 5,000,000 | 1,000 | 0 | 0 | 5,000,000 |
| 5/01/2017 | Corn swap | C-CBOT | NA | Bu | 5,000,000 | 1,000 | 0 | 0 | 5,000,000 |
| 5/02/2017 | Corn swap | C-CBOT | NA | Bu | 5,000,000 | 1,000 | 0 | 0 | 5,000,000 |
| 5/03/2017 | Corn swap | C-CBOT | NA | Bu | 5,000,000 | 1,000 | 0 | 0 | 5,000,000 |
| 5/04/2017 | Corn swap | C-CBOT | NA | Bu | 5,000,000 | 1,000 | 0 | 0 | 5,000,000 |
| 5/05/2017 | Corn swap | C-CBOT | NA | Bushels-Bu | 5,000,000 | 1,000 | 0 | 0 | 3,000,000 |

# CFTC FORM 704

# INITIAL STATEMENT AND ANNUAL UPDATE FOR ANTICIPATORY BONA FIDE HEDGING POSITIONS

**NOTICE:** Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act")[1] and the regulations thereunder,[2] or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 USC 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both.

## PRIVACY ACT NOTICE

The Commission's authority for soliciting this information is granted in sections 4a, 4c(b), 4i, 4t and 8a(5) of the CEA and related regulations (see, e.g., 17 CFR § 19.00). The information solicited from entities and individuals engaged in activities covered by the CEA is required to be provided to the CFTC, and failure to comply may result in the imposition of criminal or administrative sanctions (*see*, e.g., 7 U.S.C. §§ 9 and 13a-1, and/or 18 U.S.C. 1001). The information requested is most commonly used in the Commission's market and trade practice surveillance activities to (a) provide information concerning the size and composition of the commodity derivatives markets, (b) permit the Commission to monitor and enforce speculative position limits and (c) enhance the Commission's trade surveillance data. The requested information may be used by the Commission in the conduct of investigations and litigation and, in limited circumstances, may be made public in accordance with provisions of the CEA and other applicable laws. It may also be disclosed to other government agencies and to contract markets to meet responsibilities assigned to them by law. The information will be maintained in, and any additional disclosures will be made in accordance with, the CFTC System of Records Notices, available on www.cftc.gov.

[1] 7 U.S.C. section 1, et seq.

[2] Unless otherwise noted, the rules and regulations referenced in this notice are found in chapter 1 of title 17 of the Code of Federal Regulations; 17 CFR Chapter 1 et seq.

## BACKGROUND & INSTRUCTIONS

Applicable Regulations:

- 17 CFR § 150.7(a) specifies who must file Form 704.
- 17 CFR § 19.00(b) specifies the manner of reporting on series ’04 reports, including Form 704.
- 17 CFR § 150.7(d) specifies the information required on Form 704.
- 17 CFR § 150.7(a) specifies that initial statements on Form 704 must be filed at least 10 days in advance of the date the person expects to exceed position limits. Annual updates must be filed on Form 704 each year thereafter.

As appropriate, please follow the instructions below to generate and submit the required report or filing. Relevant regulations are cited in parentheses () for reference. Unless the context requires otherwise, the terms used herein shall have the same meaning as ascribed in parts 15 to 21 of the Commission’s regulations.

**Complete Form 704 as follows:**

**The trader identification fields should be completed by all filers.** This new Form 704 requires traders to identify themselves using their Public Trader Identification Number. This number is provided to traders who have previously filed Forms 40 and 102 with the Commission. Traders may contact the Commission to obtain this number if it is unknown. If a trader has a National Futures Association Identification Number (“NFA ID”) and/or a Legal Entity Identifier (“LEI”), he should also identify himself using those numbers. Form 704 requires traders to identify the name of the reporting trader or firm and the contact information (including full name, address, phone number, and email address) for a natural person the Commission may contact regarding the submitted Form 704.

**Form 704 must be completed by all filers who seek an exemption for anticipated bona fide hedging positions. Form 704 contains the following fields:**

| | |
|---|---|
| Initial Statement or Annual Update .......... | Select Initial Statement if filing for the first time OR Annual Update if filing an annual update to a previously filed Form 704 (§ 150.7(d)) |
| Anticipated Activity............................ | Type of anticipated activity; choose Production, Requirements, Royalty Receipts, Service Contract Payments or Receipts. Traders filing for multiple types of anticipated activity must show each type on a new line of Form 704. (§ 150.1 BFH definition paragraphs 3(iii), 4(i),4(ii), 4(iv) or (5) |
| Cash Commodity................................ | Commodity being hedged (§ 150.7 (d)(1)(i)) |
| Units............................................ | Units of measure for cash commodity being hedged |
| CRFC............................................ | Corresponding Core Referenced Futures Contract (§ 150.2(d)) |
| Same or Cross-Hedged........................ | Identify whether the cash commodity being hedged is the same as the commodity underlying the CRFC (type “S”) or whether it is a cross-hedging commodity (type “C-H”) (§ 150.7 (d)(1)(iii)) |
| Annual Activity................................. | Quantity of annual actual activity for each of the preceding three years if filing an initial statement OR the prior year if filing an annual update. If a filer does not have three years of activity to submit, she may submit a reasonable, supported estimate of anticipated production for review by Commission staff. (§ 150.7 (d)(1)(iv)(A)-(B)) |
| Specific Time Period Claimed................ | Date range for which an anticipatory exemption is being claimed, e.g. 01/01/2017 – 12/31/2017. If filing an annual update, select the amount of time remaining since the initial statement (§ 150.7 (d)(1)(v)) |
| Anticipated for Specified Time............... | Quantity of total anticipated activity over entire specified time period in futures equivalents (§ 150.7 (d)(1)(vi)) |

| | |
|---|---|
| Fixed Price Forward Activity………………… | Quantity of fixed price forward activity in cash commodity being hedged for the specified time period in futures equivalents (§ 150.7 (d)(1)(vii)) |
| Unsold, Unfilled, Anticipated Activity ……. | Unsold or unfilled anticipated production, requirements, royalty receipts, or service contract payments or receipts the risks of which have not been offset with cash positions, of such commodity for the specified time period (§ 150.7 (d)(1)(viii)) |
| Maximum Expected Position……………… | The maximum number of long or short positions in referenced contracts expected to be used to offset the risks of anticipated activity (§ 150.7 (d)(1)(ix)) |

**The signature/authorization page must be completed by all filers.** This page must include the name and position of the natural person filing Form 704 as well as the name of the reporting trader represented by that person. The trader certifying this Form 704 on the signature/authorization page should note that filing a report that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both.

***Submitting Form 704:*** Once completed, please submit this form to the Commission pursuant to the instructions on [www.cftc.gov] or as otherwise directed by Commission staff. If submission attempts fail, the reporting trader shall contact the Commission at [techsupport@cftc.gov] for further technical support.

Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

| Public Trader ID No. [provided by CFTC] | OMB No. 3038-0013 |
|---|---|

**COMMODITY FUTURES TRADING COMMISSION**
**FORM 704**
**INITIAL STATEMENT AND ANNUAL UPDATE FOR ANTICIPATORY BONA FIDE HEDGING POSITIONS**

| Identifying Information | | | |
|---|---|---|---|
| Identification Codes: | | | |
| NFA ID | Legal Entity Identifier (LEI) | | |
| | | | |
| Name of Reporting Trader or Firm: | | | |
| | | | |
| Name of Person to Contact Regarding This Form: | | | |
| First Name | Middle Name | Last Name | Suffix |
| | | | |
| Contact Information: | | | |
| Address | Phone Number | Email Address | |
| | | | |

NOTICE: Failure to file a report required by the Commodity Exchange Act ("CEA" or the "Act") and the regulations thereunder, or the filing of a report with the Commodity Futures Trading Commission ("CFTC" or "Commission") that includes a false, misleading or fraudulent statement or omits material facts that are required to be reported therein or are necessary to make the report not misleading, may (a) constitute a violation of § 6(c)(2) of the Act (7 U.S.C. 9), § 9(a)(3) of the Act (7 U.S.C. 13(a)(3)), and/or § 1001 of Title 18, Crimes and Criminal Procedure (18 U.S.C. 1001) and (b) result in punishment by fine or imprisonment, or both. Please be advised that pursuant to 5 CFR § 1320.5(b)(2)(i), you are not required to respond to this collection of information unless it displays a currently valid OMB control number.

Initial Statement and Annual Update for Anticipatory Activity pursuant to § 150.7 (d)

Check here if filing Initial Statement: ☐

Check here if filing Annual Update: ☐

| Anticipated Activity (Production, Requirements, Royalty Receipts, Service Contract Payments or Receipt) | Cash Commodity Underlying Anticipated Activity | Units for Cash Commodity (Specify Tons, CWT, Lbs., Bu., Bbls., etc.) | Core Referenced Futures contract (CRFC) | Cash Commodity Same as (S) or Cross-hedged (C-H) with Core Reference Futures Contract (CRFC) | Annual Production, Requirements, Royalty Receipts, Service Contract Payments or Receipts for Preceding Three Years (One Year if Annual Update) | Specified Time Period (Date Range) for which Anticipatory Hedge Exemption is Claimed | Anticipated Activity for Such specified Time Period in Futures Equivalent | Fixed-Price Forward sales, Inventory, and Fixed Price Forward Purchases | Unsold, Unfilled and Anticipated Activity | Maximum Number of Long or Short Positions in RC expected to be used to offset Anticipated Activity |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | | | |

CFTC Form 704 (XX-XX)

Please sign/authenticate the Form 704 prior to submitting.

Signature/ Electronic Authentication:

□ By checking this box and submitting this form (or by clicking "submit," "send," or any other analogous transmission command if transmitting electronically), I certify that I am duly authorized by the reporting trader identified below to provide the information and representations submitted on this Form 704, and that to the best of my knowledge the information and representations made herein are true and correct.

Reporting Trader Authorized Representative (Name and Position):

____________________ (Name)

____________________ (Position)

Submitted on behalf of:

____________________ (Reporting Trader Name)

Date of Submission: ____________________

CFTC Form 704 (XX-XX)

Form 704, Example A – A producer files an initial anticipatory exemption for anticipated production of crude oil for the next three years. The producer had production over the prior three calendar years (15 million, 18 million, and 20 million barrels) and is highly certain of anticipated production for the next 3 calendar years of 20 million barrels per year. The producer has no forward sales; hence, the full 60 million barrels of anticipated production (20 million barrels of anticipated production per year for three years) is unsold anticipated production. The unit of trading for the NYMEX Light Sweet Crude Oil futures contract (CL) is 1,000 barrels. The maximum hedge would be a short position of 60,000 contracts in the NYMEX CL contract.

| A. Initial Statement and Annual Update for Anticipatory Activity pursuant to § 150.7 (d) | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Check here if filing Initial Statement: ☑ | | | | | | Check here if filing Annual Update: ☐ | | | | |
| Anticipated Activity (Production, Requirements, Royalty Receipts, Service Contract Payments or Receipt) | Cash Commodity Underlying Anticipated Activity | Units for Cash Commodity (Specify Tons, CWT, Lbs., Bu., Bbls., etc.) | Core Referenced Futures contract (CRFC) | Cash Commodity Same as (S) or Cross-hedged (C-H) with Core Reference Futures Contract (CRFC) | Annual Production, Requirements, Royalty Receipts, Service Contract Payments or Receipts for Preceding Three Years (One Year if Annual Update) | Specified Time Period (Date Range) for which Anticipatory Hedge Exemption is Claimed | Anticipated Activity for Such specified Time Period in Futures Equivalent | Fixed-Price Forward sales, Inventory, and Fixed Price Forward Purchases | Unsold, Unfilled and Anticipated Activity | Maximum Number of Long or Short Positions in RC expected to be used to offset Anticipated Activity |
| Production | Crude Oil | (m='000,000) bbls | CL-NYMEX | S | 2014-15m<br>2015-18m<br>2016-20m | 1/1/2017 – 12/31/2019 | 60,000 | 0 | 60,000 | -60,000 |
| | | | | | | | | | | |

Form 704, Example B. In 2018, one year after filing the initial statement, the producer in Example A files an annual update. Actual production for the prior year was 20 million barrels, as forecasted. The producer remains highly certain of 40 million barrels of production (20 million barrels of crude oil for each of the next two years). The producer has sold forward 10 million barrels. Hence, remaining unsold anticipated production is 30 million barrels. The maximum hedge would be a short position of 30,000 contracts in the NYMEX CL contract.

| A. Initial Statement and Annual Update for Anticipatory Activity pursuant to § 150.7 (d) | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Check here if filing Initial Statement: ☐ | | | | | | Check here if filing Annual Update: ☑ | | | | | |
| Anticipated Activity (Production, Requirements, Royalty Receipts, Service Contract Payments or Receipt) | Type and Name of Cash Commodity Underlying Anticipated Activity | Units for Cash Commodity (Specify Tons, CWT, Lbs., Bu., Bbls., etc.) | Core Referenced Futures contract (CRFC) | Cash Commodity Same as (S) or Cross-hedged (C-H) with Core Reference Futures Contract (CRFC) | Annual Production, Requirements, Royalty Receipts, Service Contract Payments or Receipts for Preceding Three Years (One Year if Annual Update) | Specified Time Period for which Anticipatory Hedge Exemption is Claimed | Anticipated Activity for Such specified Time Period in Futures Equivalent | Fixed-Price Forward sales, Inventory, and Fixed Price Forward Purchases | Unsold, Unfilled and Anticipated Activity | Maximum Number of Long or Short Positions in RC expected to be used to offset Anticipated Activity |
| Production | Crude Oil | (m='000,000) bbls | CL-NYMEX | S | 2017-20m | 2 years | 40,000 | -10,000 | 30,000 | -30,000 |

BILLING CODE 6351–01–C

## PART 37—SWAP EXECUTION FACILITIES

■ 13. The authority citation for part 37 continues to read as follows:

**Authority:** 7 U.S.C. 1a, 2, 5, 6, 6c, 7, 7a–2, 7b–3, and 12a, as amended by Titles VII and VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111–203, 124 Stat. 1376.

■ 14. Revise § 37.601 to read as follows:

### § 37.601 Additional sources for compliance.

A swap execution facility that is a trading facility must meet the requirements of part 150 of this chapter, as applicable.

■ 15. In Appendix B to part 37, under the heading Core Principle 6 of Section 5h of the Act—Position Limits or Accountability, revise paragraphs (A) and (B) to read as follows:

### Appendix B to Part 37—Guidance on, and Acceptable Practices in, Compliance with Core Principles

* * * * *

#### Core Principle 6 of Section 5h of the Act—Position Limits or Accountability

(A) *In general.* To reduce the potential threat of market manipulation or congestion, especially during trading in the delivery month, a swap execution facility that is a trading facility shall adopt for each of the contracts of the facility, as is necessary and appropriate, position limitations or position accountability for speculators.

(B) *Position limits.* For any contract that is subject to a position limitation established by the Commission pursuant to section 4a(a), the swap execution facility shall:

(1) Set its position limitation at a level not higher than the Commission limitation; and

(2) Monitor positions established on or through the swap execution facility for compliance with the limit set by the Commission and the limit, if any, set by the swap execution facility.

(a) *Guidance.*

(1) Until a swap execution facility has access to sufficient swap position information, a swap execution facility that is a trading facility need not demonstrate compliance with Core Principle 6(B). A swap execution facility has access to sufficient swap position information if, for example:

(i) It has access to daily information about its market participants' open swap positions; or

(ii) It knows, including through knowledge gained in surveillance of heavy trading activity occurring on or pursuant to the rules of the swap execution facility, that its market participants regularly engage in large volumes of speculative trading activity that would cause reasonable surveillance personnel at a swap execution facility to inquire further about a market participant's intentions or open swap positions.

(2) When a swap execution facility has access to sufficient swap position information, this guidance is no longer applicable. At such time, a swap execution facility is required to demonstrate compliance with Core Principle 6(B).

(b) *Acceptable practices.* [Reserved]

* * * * *

## PART 38—DESIGNATED CONTRACT MARKETS

■ 16. The authority citation for part 38 continues to read as follows:

**Authority:** 7 U.S.C. 1a, 2, 6, 6a, 6c, 6d, 6e, 6f, 6g, 6i, 6j, 6k, 6l, 6m, 6n, 7, 7a–2, 7b, 7b–1, 7b–3, 8, 9, 15, and 21, as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111–203, 124 Stat. 1376.

■ 17. Revise § 38.301 to read as follows:

### § 38.301 Position limitations and accountability.

A designated contract market must meet the requirements of part 150 of this chapter, as applicable.

■ 18. In Appendix B to part 38, under the heading Core Principle 5 of section 5(d) of the Act: Position Limitations or Accountability, revise paragraphs (A) and (B) to read as follows:

### Appendix B to Part 38—Guidance on, and Acceptable Practices in, Compliance with Core Principles

* * * * *

#### Core Principle 5 of Section 5(d) of the Act: Position Limitations or Accountability

(A) *In general.*—To reduce the potential threat of market manipulation or congestion (especially during trading in the delivery month), the board of trade shall adopt for each contract of the board of trade, as is necessary and appropriate, position limitations or position accountability for speculators.

(B) *Maximum allowable position limitation.*—For any contract that is subject to a position limitation established by the Commission pursuant to section 4a(a), the board of trade shall set the position limitation of the board of trade at a level not higher than the position limitation established by the Commission.

(a) *Guidance.*

(1) Until a board of trade has access to sufficient swap position information, a board of trade need not demonstrate compliance with Core Principle 5(B) with respect to swaps. A board of trade has access to sufficient swap position information if, for example:

(i) It has access to daily information about its market participants' open swap positions; or

(ii) It knows, including through knowledge gained in surveillance of heavy trading activity occurring on or pursuant to the rules of the designated contract market, that its market participants regularly engage in large volumes of speculative trading activity that would cause reasonable surveillance personnel at a board of trade to inquire further about a market participant's intentions or open swap positions.

(2) When a board of trade has access to sufficient swap position information, this guidance is no longer applicable. At such time, a board of trade is required to demonstrate compliance with Core Principle 5(B) with respect to swaps.

(b) *Acceptable Practices.* [Reserved]

* * * * *

## PART 140—ORGANIZATION, FUNCTIONS, AND PROCEDURES OF THE COMMISSION

■ 19. The authority citation for part 140 continues to read as follows:

**Authority:** 7 U.S.C. 2(a)(12), 12a, 13(c), 13(d), 13(e), and 16(b).

### § 140.97 [Removed and reserved]

■ 20. Remove and reserve § 140.97.

## PART 150—LIMITS ON POSITIONS

■ 21. The authority citation for part 150 continues to read as follows:

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

■ 22. Revise § 150.1 to read as follows:

### § 150.1 Definitions.

As used in this part—

*Bona fide hedging position* means—

(1) *Hedges of an excluded commodity.* For a position in commodity derivative contracts in an excluded commodity, as that term is defined in section 1a(19) of the Act:

(i) Such position is economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise and is enumerated in paragraph (3), (4) or (5) of this definition; or

(ii) Is otherwise recognized as a bona fide hedging position by the designated contract market or swap execution facility that is a trading facility, pursuant to such market's rules submitted to the Commission, which rules may include risk management exemptions consistent with Appendix A of this part; and

(2) *Hedges of a physical commodity—general definition.* For a position in commodity derivative contracts in a physical commodity:

(i) Such position:

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

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

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

(*1*) Assets which a person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising;

(*2*) Liabilities which a person owes or anticipates incurring; or

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

(ii)(A) *Pass-through swap offsets.* Such position reduces risks attendant to a position resulting from a swap in the same physical commodity that was executed opposite a counterparty for which the swap would qualify as a bona fide hedging position pursuant to paragraph (2)(i) of this definition (a pass-through swap counterparty), *provided that* the bona fides of the pass-through swap counterparty may be determined at the time of the transaction;

(B) *Pass-through swaps.* Such swap position was executed opposite a pass-through swap counterparty and to the extent such swap position has been offset pursuant to paragraph (2)(ii)(A) of this definition; or

(C) *Offsets of bona fide hedging swap positions.* Such position reduces risks attendant to a position resulting from a swap that meets the requirements of paragraph (2)(i) of this definition.

(iii) *Additional requirements for enumeration or other recognition.* Notwithstanding the foregoing general definition, a position in commodity derivative contracts in a physical commodity shall be classified as a bona fide hedging position only if:

(A) The position satisfies the requirements of paragraph (2)(i) of this definition and is enumerated in paragraph (3), (4), or (5) of this definition;

(B) The position satisfies the requirements of paragraph (2)(ii) of this definition, *provided that* no offsetting position is maintained in any physical-delivery commodity derivative contract during the lesser of the last five days of trading or the time period for the spot month in such physical-delivery commodity derivative contract; or

(C) The position has been otherwise recognized as a non-enumerated bona fide hedging position by either a designated contract market or swap execution facility, each in accordance with § 150.9(a); or by the Commission.

(3) *Enumerated hedging positions.* A bona fide hedging position includes any of the following specific positions:

(i) *Hedges of inventory and cash commodity purchase contracts.* Short positions in commodity derivative contracts that do not exceed in quantity ownership or fixed-price purchase contracts in the contract's underlying cash commodity by the same person.

(ii) *Hedges of cash commodity sales contracts.* Long positions in commodity derivative contracts that do not exceed in quantity the fixed-price sales contracts in the contract's underlying cash commodity by the same person and the quantity equivalent of fixed-price sales contracts of the cash products and by-products of such commodity by the same person.

(iii) *Hedges of unfilled anticipated requirements. Provided that* such positions in a physical-delivery commodity derivative contract, during the lesser of the last five days of trading or the time period for the spot month in such physical-delivery contract, do not exceed the person's unfilled anticipated requirements of the same cash commodity for that month and for the next succeeding month:

(A) Long positions in commodity derivative contracts that do not exceed in quantity unfilled anticipated requirements of the same cash commodity, for processing, manufacturing, or use by the same person; and

(B) Long positions in commodity derivative contracts that do not exceed in quantity unfilled anticipated requirements of the same cash commodity for resale by a utility to its customers.

(iv) *Hedges by agents.* Long or short positions in commodity derivative contracts by an agent who does not own or has not contracted to sell or purchase the offsetting cash commodity at a fixed price, *provided that* the agent is responsible for merchandising the cash positions that are being offset in commodity derivative contracts and the agent has a contractual arrangement with the person who owns the commodity or holds the cash market commitment being offset.

(4) *Other enumerated hedging positions.* A bona fide hedging position also includes the following specific positions, *provided that* no such position is maintained in any physical-delivery commodity derivative contract during the lesser of the last five days of trading or the time period for the spot month in such physical-delivery contract:

(i) *Hedges of unsold anticipated production.* Short positions in commodity derivative contracts that do not exceed in quantity unsold anticipated production of the same commodity by the same person.

(ii) *Hedges of offsetting unfixed-price cash commodity sales and purchases.* Short and long positions in commodity derivative contracts that do not exceed in quantity that amount of the same cash commodity that has been bought and sold by the same person at unfixed prices:

(A) Basis different delivery months in the same commodity derivative contract; or

(B) Basis different commodity derivative contracts in the same commodity, regardless of whether the commodity derivative contracts are in the same calendar month.

(iii) *Hedges of anticipated royalties.* Short positions in commodity derivative contracts offset by the anticipated change in value of mineral royalty rights that are owned by the same person, *provided that* the royalty rights arise out of the production of the commodity underlying the commodity derivative contract.

(iv) *Hedges of services.* Short or long positions in commodity derivative contracts offset by the anticipated change in value of receipts or payments due or expected to be due under an executed contract for services held by the same person, *provided that* the contract for services arises out of the production, manufacturing, processing, use, or transportation of the commodity underlying the commodity derivative contract.

(5) *Cross-commodity hedges.* Positions in commodity derivative contracts described in paragraph (2)(ii), paragraphs (3)(i) through (iv) and paragraphs (4)(i) through (iv) of this definition may also be used to offset the risks arising from a commodity other than the same cash commodity underlying a commodity derivative contract, *provided that* the fluctuations in value of the position in the commodity derivative contract, or the commodity underlying the commodity derivative contract, are substantially related to the fluctuations in value of the actual or anticipated cash position or pass-through swap and no such position is maintained in any physical-delivery commodity derivative contract during the lesser of the last five days of trading or the time period for the spot month in such physical-delivery contract.

(6) *Offsets of commodity trade options.* For purposes of this definition, a commodity trade option, meeting the requirements of § 32.3 of this chapter for a commodity option transaction, may be deemed a cash commodity purchase or sales contract, as appropriate, *provided that* such option is adjusted on a futures-equivalent basis. By way of example, a commodity trade option with a fixed strike price may be converted to a futures-equivalent basis, and, on that futures-equivalent basis,

deemed a cash commodity sale, in the case of a short call option or long put option, or a cash commodity purchase, in the case of a long call option or short put option.

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

*Commodity derivative contract* means, for this part, any futures, option, or swap contract in a commodity (other than a security futures product as defined in section 1a(45) of the Act).

*Commodity index contract* means an agreement, contract, or transaction that is not a location basis contract or any type of spread contract, based on an index comprised of prices of commodities that are not the same or substantially the same.

*Core referenced futures contract* means a futures contract that is listed in § 150.2(d).

*Eligible affiliate.* An eligible affiliate means an entity with respect to which another person:

(1) Directly or indirectly holds either:

(i) A majority of the equity securities of such entity, or

(ii) The right to receive upon dissolution of, or the contribution of, a majority of the capital of such entity;

(2) Reports its financial statements on a consolidated basis under Generally Accepted Accounting Principles or International Financial Reporting Standards, and such consolidated financial statements include the financial results of such entity; and

(3) Is required to aggregate the positions of such entity under § 150.4 and does not claim an exemption from aggregation for such entity.

*Eligible entity*[1] means a commodity pool operator, the operator of a trading vehicle which is excluded or who itself has qualified for exclusion from the definition of the term ''pool'' or ''commodity pool operator,'' respectively, under § 4.5 of this chapter; the limited partner or shareholder in a commodity pool the operator of which is exempt from registration under § 4.13 of this chapter; a commodity trading advisor; a bank or trust company; a savings association; an insurance company; or the separately organized affiliates of any of the above entities:

(1) Which authorizes an independent account controller independently to control all trading decisions for positions it holds directly or indirectly, or on its behalf, but without its day-to-day direction; and

(2) Which maintains:

(i) Only such minimum control over the independent account controller as is consistent with its fiduciary responsibilities and necessary to fulfill its duty to supervise diligently the trading done on its behalf; or

(ii) If a limited partner or shareholder of a commodity pool the operator of which is exempt from registration under § 4.13 of this chapter, only such limited control as is consistent with its status.

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

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

*Futures-equivalent* means

(1) An option contract, whether an option on a future or an option that is a swap, which has been adjusted by an economically reasonable and analytically supported risk factor, or delta coefficient, for that option computed as of the previous day's close or the current day's close or contemporaneously during the trading day, and converted to an economically equivalent amount of an open position in a core referenced futures contract, *provided however,* if a participant's position exceeds position limits as a result of an option assignment, that participant is allowed one business day to liquidate the excess position without being considered in violation of the limits;

(2) A futures contract which has been converted to an economically equivalent amount of an open position in a core referenced futures contract; and

(3) A swap which has been converted to an economically equivalent amount of an open position in a core referenced futures contract.

*Independent account controller*[2] means a person—

(1) Who specifically is authorized by an eligible entity, as defined in this section, independently to control trading decisions on behalf of, but without the day-to-day direction of, the eligible entity;

(2) Over whose trading the eligible entity maintains only such minimum control as is consistent with its fiduciary responsibilities to fulfill its duty to supervise diligently the trading done on its behalf or as is consistent with such other legal rights or obligations which may be incumbent upon the eligible entity to fulfill;

(3) Who trades independently of the eligible entity and of any other independent account controller trading for the eligible entity;

(4) Who has no knowledge of trading decisions by any other independent account controller; and

(5) Who is registered as a futures commission merchant, an introducing broker, a commodity trading advisor, an associated person or any such registrant, or is a general partner of a commodity pool the operator of which is exempt from registration under § 4.13 of this chapter.

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

*Intermarket spread position* means a long (short) position in one or more commodity derivative contracts in a particular commodity, or its products or its by-products, at a particular designated contract market or swap execution facility and a short (long) position in one or more commodity derivative contracts in that same, or similar, commodity, or its products or its by-products, away from that particular designated contract market or swap execution facility.

*Intramarket spread position* means a long position in one or more commodity derivative contracts in a particular commodity, or its products or its by-products, and a short position in one or more commodity derivative contracts in the same, or similar, commodity, or its products or its by-products, on the same designated contract market or swap execution facility.

*Location basis contract* means a commodity derivative contract that is cash-settled based on the difference in:

(1) The price, directly or indirectly, of:

(i) A particular core referenced futures contract; or

[1] The definition of the term, eligible entity, was amended by the Commission in a final rule published on December 16, 2016 (81 FR 91454, 91489). The unamended version of the definition presented here is included solely to maintain the continuity of this regulatory section and for the convenience of the reader. The definition of the term, eligible entity, is not a subject of this reproposal and will be revised when the amended definition takes effect on February 14, 2017.

[2] The definition of the term, independent account controller, was amended by the Commission in a final rule published on December 16, 2016 (81 FR 91454, 91489). The unamended version of the definition presented here is included solely to maintain the continuity of this regulatory section and for the convenience of the reader. The definition of the term, independent account controller, is not a subject of this reproposal and will be revised when the amended definition takes effect on February 14, 2017.

(ii) A commodity deliverable on a particular core referenced futures contract, whether at par, a fixed discount to par, or a premium to par; and

(2) The price, at a different delivery location or pricing point than that of the same particular core referenced futures contract, directly or indirectly, of:

(i) A commodity deliverable on the same particular core referenced futures contract, whether at par, a fixed discount to par, or a premium to par; or

(ii) A commodity that is listed in Appendix B to this part as substantially the same as a commodity underlying the same core referenced futures contract.

*Long position* means, on a futures-equivalent basis, a long call option, a short put option, a long underlying futures contract, or a swap position that is equivalent to a long futures contract.

*Physical commodity* means any agricultural commodity as that term is defined in § 1.3 of this chapter or any exempt commodity as that term is defined in section 1a(20) of the Act.

*Pre-enactment swap* means any swap entered into prior to enactment of the Dodd-Frank Act of 2010 (July 21, 2010), the terms of which have not expired as of the date of enactment of that Act.

*Pre-existing position* means any position in a commodity derivative contract acquired in good faith prior to the effective date of any bylaw, rule, regulation or resolution that specifies an initial speculative position limit level or a subsequent change to that level.

*Referenced contract* means a core referenced futures contract listed in § 150.2(d) or, on a futures equivalent basis with respect to a particular core referenced futures contract, a futures contract, options contract, or swap that is:

(1) Directly or indirectly linked, including being partially or fully settled on, or priced at a fixed differential to, the price of that particular core referenced futures contract; or

(2) Directly or indirectly linked, including being partially or fully settled on, or priced at a fixed differential to, the price of the same commodity underlying that particular core referenced futures contract for delivery at the same location or locations as specified in that particular core referenced futures contract.

(3) The definition of referenced contract does not include any guarantee of a swap, a location basis contract, a commodity index contract, or a trade option that meets the requirements of § 32.3 of this chapter.

*Short position* means, on a futures-equivalent basis, a short call option, a long put option, a short underlying futures contract, or a swap position that is equivalent to a short futures contract.

*Speculative position limit* means the maximum position, either net long or net short, in a commodity derivatives contract that may be held or controlled by one person, absent an exemption, such as an exemption for a bona fide hedging position. This limit may apply to a person's combined position in all commodity derivative contracts in a particular commodity (all-months-combined), a person's position in a single month of commodity derivative contracts in a particular commodity, or a person's position in the spot month of commodity derivative contacts in a particular commodity. Such a limit may be established under federal regulations or rules of a designated contract market or swap execution facility. An exchange may also apply other limits, such as a limit on gross long or gross short positions, or a limit on holding or controlling delivery instruments.

*Spot month* means—

(1) For physical-delivery core referenced futures contracts, the period of time beginning at the earlier of the close of business on the trading day preceding the first day on which delivery notices can be issued by the clearing organization of a contract market, or the close of business on the trading day preceding the third-to-last trading day, until the contract expires, except as follows:

(i) For *ICE Futures U.S. Sugar No. 11* (SB) referenced contract, the spot month means the period of time beginning at the opening of trading on the second business day following the expiration of the regular option contract traded on the expiring futures contract until the contract expires;

(ii) For *ICE Futures U.S. Sugar No. 16* (SF) referenced contract, the spot month means the period of time beginning on the third-to-last trading day of the contract month until the contract expires;

(iii) For *Chicago Mercantile Exchange Live Cattle* (LC) referenced contract, the spot month means the period of time beginning at the close trading on the fifth business day of the contract month until the contract expires;

(2) For cash-settled core referenced futures contracts:

(i) [Reserved]

(3) For referenced contracts other than core referenced futures contracts, the spot month means the same period as that of the relevant core referenced futures contract.

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

*Swap* means ''swap'' as that term is defined in section 1a of the Act and as further defined in § 1.3 of this chapter.

*Swap dealer* means ''swap dealer'' as that term is defined in section 1a of the Act and as further defined in § 1.3 of this chapter.

*Transition period swap* means a swap entered into during the period commencing after the enactment of the Dodd-Frank Act of 2010 (July 21, 2010), and ending 60 days after the publication in the **Federal Register** of final amendments to this part implementing section 737 of the Dodd-Frank Act of 2010.

■ 23. Revise § 150.2 to read as follows:

**§ 150.2 Speculative position limits.**

(a) *Spot-month speculative position limits.* No person may hold or control positions in referenced contracts in the spot month, net long or net short, in excess of the level specified by the Commission for:

(1) Physical-delivery referenced contracts; and, separately,

(2) Cash-settled referenced contracts;

(b) *Single-month and all-months-combined speculative position limits.* No person may hold or control positions, net long or net short, in referenced contracts in a single month or in all months combined (including the spot month) in excess of the levels specified by the Commission.

(c) For purposes of this part:

(1) The spot month and any single month shall be those of the core referenced futures contract; and

(2) An eligible affiliate is not required to comply separately with speculative position limits.

(d) *Core referenced futures contracts.* Speculative position limits apply to referenced contracts based on the core referenced futures contracts listed in Table Core Referenced Futures Contracts:

CORE REFERENCED FUTURES CONTRACTS

| Commodity type | Designated contract market | Core referenced futures contract [1] |
|---|---|---|
| Legacy Agricultural | Chicago Board of Trade | Corn (C). |

CORE REFERENCED FUTURES CONTRACTS—Continued

| Commodity type | Designated contract market | Core referenced futures contract [1] |
|---|---|---|
| | | Oats (O). |
| | | Soybeans (S). |
| | | Soybean Meal (SM). |
| | | Soybean Oil (SO). |
| | | Wheat (W). |
| | | Hard Winter Wheat (KW). |
| | ICE Futures U.S. | Cotton No. 2 (CT). |
| | Minneapolis Grain Exchange | Hard Red Spring Wheat (MWE). |
| Other Agricultural | Chicago Board of Trade | Rough Rice (RR). |
| | Chicago Mercantile Exchange | Live Cattle (LC). |
| | ICE Futures U.S. | Cocoa (CC). |
| | | Coffee C (KC). |
| | | FCOJ–A (OJ). |
| | | U.S. Sugar No. 11 (SB). |
| | | U.S. Sugar No. 16 (SF). |
| Energy | New York Mercantile Exchange | Light Sweet Crude Oil (CL). |
| | | NY Harbor ULSD (HO). |
| | | RBOB Gasoline (RB). |
| | | Henry Hub Natural Gas (NG). |
| Metals | Commodity Exchange, Inc. | Gold (GC). |
| | | Silver (SI). |
| | | Copper (HG). |
| | New York Mercantile Exchange | Palladium (PA). |
| | | Platinum (PL). |

[1] The core referenced futures contract includes any successor contracts.

(e) *Levels of speculative position limits*—(1) *Initial levels.* The initial levels of speculative position limits are fixed by the Commission at the levels listed in Appendix D to this part; *provided however,* compliance with such initial speculative limits shall not be required until January 3, 2018, which date shall be the initial establishment date for purposes of paragraphs (e)(3) and (4) of this section.

(2) *Subsequent levels.* (i) The Commission shall fix subsequent levels of speculative position limits in accordance with the procedures in this section and publish such levels on the Commission's Web site at *http://www.cftc.gov.*

(ii) Such subsequent speculative position limit levels shall each apply beginning on the close of business of the last business day of the second complete calendar month after publication of such levels; *provided however,* if such close of business is in a spot month of a core referenced futures contract, the subsequent spot-month level shall apply beginning with the next spot month for that contract.

(iii) All subsequent levels of speculative position limits shall be rounded up to the nearest hundred contracts.

(3) *Procedure for computing levels of spot-month limits.* (i) No less frequently than every two calendar years, the Commission shall fix the level of the spot-month limit no greater than one-quarter of the estimated spot-month deliverable supply in the relevant core referenced futures contract. Unless the Commission determines to rely on its own estimate of deliverable supply, the Commission shall utilize the estimated spot-month deliverable supply provided by a designated contract market. If the Commission determines to rely on its own estimate of deliverable supply, then the Commission shall publish such estimate for public comment in the **Federal Register**; provided however, that the Commission may determine to fix the level of the spot-month limit at a level, recommended by the designated contract market listing the relevant core referenced futures contract for good cause shown, that is less than one-quarter of the estimated spot-month deliverable supply, or not to change the level of the spot-month limit.

(ii) *Estimates of deliverable supply.* (A) Each designated contract market in a core referenced futures contract shall supply to the Commission an estimated spot-month deliverable supply. A designated contract market may use the guidance regarding deliverable supply in Appendix C to part 38 of this chapter. Each estimate must be accompanied by a description of the methodology used to derive the estimate and any statistical data supporting the estimate, and must be submitted no later than the following:

(*1*) For energy commodities, January 31 of the second calendar year following the most recent Commission action establishing such limit levels;

(*2*) For metals commodities, March 31 of the second calendar year following the most recent Commission action establishing such limit levels;

(*3*) For legacy agricultural commodities, May 31 of the second calendar year following the most recent Commission action establishing such limit levels; and

(*4*) For other agricultural commodities, August 31 of the second calendar year following the most recent Commission action establishing such limit levels.

(B) Notwithstanding paragraph (e)(3)(ii)(A) of this section, each designated contract market may petition the Commission not less than two calendar months before the due date for submission of an estimate of deliverable supply under paragraph (e)(3)(ii)(A) of this section, recommending that the Commission not change the spot-month limit. Such recommendation should include a summary of the designated contract market's experience administering its spot-month limit. The Commission shall determine not less than one calendar month before such due date whether to accept the designated contract market's recommendation. If the Commission accepts such recommendation, then the designated contract market need not submit an estimated spot-month deliverable supply for such due date.

(4) *Procedure for computing levels of single-month and all-months-combined limits.* No less frequently than every two calendar years, the Commission shall fix the level, for each referenced contract, of the single-month limit and the all-

months-combined limit. Each such limit shall be based on 10 percent of the estimated average open interest in referenced contracts, up to 25,000 contracts, with a marginal increase of 2.5 percent thereafter; *provided however,* the Commission may determine not to change the level of the single-month limit or the all-months-combined limit.

(i) *Time periods for average open interest.* The Commission shall estimate average open interest in referenced contracts based on the largest annual average open interest computed for each of the past two calendar years. The Commission may estimate average open interest in referenced contracts using either month-end open contracts or open contracts for each business day in the time period, as practical.

(ii) *Data sources for average open interest.* The Commission shall estimate average open interest in referenced contracts using data reported to the Commission pursuant to part 16 of this chapter, and open swaps reported to the Commission pursuant to part 20 of this chapter or data obtained by the Commission from swap data repositories collecting data pursuant to part 45 of this chapter. Options listed on designated contract markets shall be adjusted using an option delta reported to the Commission pursuant to part 16 of this chapter. Swaps shall be counted on a futures equivalent basis, equal to the economically equivalent amount of core referenced futures contracts reported pursuant to part 20 of this chapter or as calculated by the Commission using swap data collected pursuant to part 45 of this chapter.

(iii) *Publication of average open interest.* The Commission shall publish estimates of average open interest in referenced contracts on a monthly basis, as practical, after such data is submitted to the Commission.

(iv) *Minimum levels. Provided however,* notwithstanding the above, the minimum levels shall be the greater of the level of the spot month limit determined under paragraph (e)(3) of this section or 5,000 contracts.

(f) *Pre-existing positions*—(1) *Pre-existing positions in a spot-month.* Other than pre-enactment and transition period swaps exempted under § 150.3(d), a person shall comply with spot month speculative position limits.

(2) *Pre-existing positions in a non-spot-month.* A single-month or all-months-combined speculative position limit established under this section shall not apply to any commodity derivative contract acquired in good faith prior to the effective date of such limit, *provided however,* that if such position is not a pre-enactment or transition period swap then that position shall be attributed to the person if the person's position is increased after the effective date of such limit.

(g) *Positions on foreign boards of trade.* The aggregate speculative position limits established under this section shall apply to a person with positions in referenced contracts executed on, or pursuant to the rules of a foreign board of trade, *provided that:*

(1) Such referenced contracts settle against any price (including the daily or final settlement price) of one or more contracts listed for trading on a designated contract market or swap execution facility that is a trading facility; and

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

(h) *Anti-evasion provision.* For the purposes of applying the speculative position limits in this section, a commodity index contract used to circumvent speculative position limits shall be considered to be a referenced contract.

(i) *Delegation of authority to the Director of the Division of Market Oversight.* (1) The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director may designate from time to time, the authority in paragraph (e) of this section to fix and publish subsequent levels of speculative position limits, including the authority not to change levels of such limits, and the authority in paragraph (e)(3)(iii) of this section to relieve a designated contract market from the requirement to submit an estimate of deliverable supply.

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

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

(j) The Commission will periodically update these initial levels for speculative position limits and publish such subsequent levels on its Web site at: *http://www.cftc.gov.*

■ 24. Revise § 150.3 to read as follows:

### § 150.3 Exemptions.

(a) *Positions which may exceed limits.* The position limits set forth in § 150.2 may be exceeded to the extent that:

(1) Such positions are:

(i) Bona fide hedging positions that comply with the definition in § 150.1, *provided that:*

(A) For non-enumerated bona fide hedges, the person has not otherwise been notified by the Commission under § 150.9(d)(4) or, under rules adopted pursuant to § 150.9(a)(4)(iv)(B), by the designated contract market or swap execution facility; and

(B) For anticipatory bona fide hedging positions under paragraphs (3)(iii), (4)(i), (4)(iii), (4)(iv) and (5) of the bona fide hedging position definition in § 150.1, the person complies with the filing requirements found in § 150.7 or the filing requirements adopted, in accordance with § 150.11(a)(3), by a designated contract market or swap execution facility, as applicable;

(ii) Financial distress positions exempted under paragraph (b) of this section;

(iii) Conditional spot-month limit positions exempted under paragraph (c) of this section;

(iv) Spread positions recognized by a designated contract market or swap execution facility, each in accordance with § 150.10(a), or the Commission, *provided that* the person has not otherwise been notified by the Commission under § 150.10(d)(4) or by the designated contract market or swap execution facility under rules adopted pursuant to § 150.10(a)(4)(iv)(B); or

(v) Other positions exempted under paragraph (e) of this section; and that

(2) The recordkeeping requirements of paragraph (g) of this section are met; and further that

(3) The reporting requirements of part 19 of this chapter are met.

(b) *Financial distress exemptions.* Upon specific request made to the Commission, the Commission may exempt a person or related persons under financial distress circumstances for a time certain from any of the requirements of this part. Financial distress circumstances include situations involving the potential default or bankruptcy of a customer of the requesting person or persons, an affiliate of the requesting person or persons, or a potential acquisition target of the requesting person or persons.

(c) *Conditional spot-month limit exemption.* The position limit set forth in § 150.2 may be exceeded for natural gas cash-settled referenced contracts, *provided* that such positions do not exceed 10,000 contracts and the person holding or controlling such positions does not hold or control positions in spot-month physical-delivery referenced contracts.

(d) *Pre-enactment and transition period swaps exemption.* The speculative position limits set forth in § 150.2 shall not apply to positions acquired in good faith in any pre-enactment swap, or in any transition period swap, in either case as defined by § 150.1; *provided however,* that a person may net such positions with post-effective date commodity derivative contracts for the purpose of complying with any non-spot-month speculative position limit.

(e) *Other exemptions.* Any person engaging in risk-reducing practices commonly used in the market, which they believe may not be specifically enumerated in the definition of bona fide hedging position in § 150.1, may request:

(1) An interpretative letter from Commission staff, under § 140.99 of this chapter, concerning the applicability of the bona fide hedging position exemption; or

(2) Exemptive relief from the Commission under section 4a(a)(7) of the Act.

(3) Appendix C to this part provides a non-exhaustive list of examples of bona fide hedging positions as defined under § 150.1.

(f) *Previously granted exemptions.* (1) Exemptions granted by the Commission under § 1.47 of this chapter for risk management of positions in financial instruments shall not apply to positions in financial instruments entered into after the effective date of initial position limits implementing section 737 of the Dodd-Frank Act of 2010.

(2) Exemptions for risk management of positions in financial instruments granted by a designated contract market or swap execution facility shall not apply to positions in financial instruments entered into after the effective date of initial position limits implementing section 737 of the Dodd-Frank Act of 2010, *provided that,* for positions in financial instruments entered into on or before the effective date of initial position limits implementing section 737 of the Dodd-Frank Act of 2010, the exemption shall apply for purposes of position limits under § 150.2 if the exemption:

(i) Applies to positions outside of the spot month only; and

(ii) Was granted prior to the compliance date provided under § 150.2(e)(1).

(g) *Recordkeeping.* (1) Persons who avail themselves of exemptions under this section, including exemptions granted under section 4a(a)(7) of the Act, shall keep and maintain complete books and records concerning all details of their related cash, forward, futures, futures options and swap positions and transactions, including anticipated requirements, production and royalties, contracts for services, cash commodity products and by-products, and cross-commodity hedges, and shall make such books and records, including a list of pass-through swap counterparties, available to the Commission upon request under paragraph (h) of this section.

(2) Further, a party seeking to rely upon the pass-through swap offset in paragraph (2)(B) of the definition of ''bona fide hedging position'' in § 150.1, in order to exceed the position limits of § 150.2 with respect to such a swap, may only do so if its counterparty provides a written representation (*e.g.,* in the form of a field or other representation contained in a mutually executed trade confirmation) that, as to such counterparty, the swap qualifies in good faith as a ''bona fide hedging position,'' as defined in § 150.1, *provided that* the bona fides of the pass-through swap counterparty may be determined at the time of the transaction. That written representation shall be retained by the parties to the swap for a period of at least two years following the expiration of the swap and furnished to the Commission upon request.

(3) Any person that represents to another person that a swap qualifies as a pass-through swap under paragraph (2)(ii)(B) of the definition of ''bona fide hedging position'' in § 150.1 shall keep and make available to the Commission upon request all relevant books and records supporting such a representation for a period of at least two years following the expiration of the swap.

(h) *Call for information.* Upon call by the Commission, the Director of the Division of Market Oversight or the Director's delegee, any person claiming an exemption from speculative position limits under this section must provide to the Commission such information as specified in the call relating to the positions owned or controlled by that person; trading done pursuant to the claimed exemption; the commodity derivative contracts or cash market positions which support the claim of exemption; and the relevant business relationships supporting a claim of exemption.

(i) *Aggregation of accounts.* Entities required to aggregate accounts or positions under § 150.4 of this part shall be considered the same person for the purpose of determining whether they are eligible for a bona fide hedging position exemption under paragraph (a)(1)(i) of this section with respect to such aggregated account or position.

(j) *Delegation of authority to the Director of the Division of Market Oversight.* (1) The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director may designate from time to time, the authority in paragraph (b) of this section to provide exemptions in circumstances of financial distress.

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

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

■ 25. Revise § 150.5 to read as follows:

**§ 150.5 Exchange-set position limits.**

(a) *Requirements and acceptable practices for commodity derivative contracts subject to federal position limits.* (1) For any commodity derivative contract that is subject to a speculative position limit under § 150.2, a designated contract market or swap execution facility that is a trading facility shall set a speculative position limit no higher than the level specified in § 150.2.

(2) *Exemptions to exchange-set limits*—(i) *Grant of exemption.* Any designated contract market or swap execution facility that is a trading facility may grant exemptions from any speculative position limits it sets under paragraph (a)(1) of this section, *provided that* exemptions from federal limits conform to the requirements specified in § 150.3, *and provided further* that any exemptions to exchange-set limits not conforming to § 150.3 are capped at the level of the applicable federal limit in § 150.2.

(ii) *Application for exemption.* Any designated contract market or swap execution facility that grants exemptions under paragraph (a)(2)(i) of this section:

(A) Must require traders to file an application requesting such exemption in advance of the date that such position would be in excess of the limits then in effect, *provided however,* that it may adopt rules that allow a trader to file an application for an enumerated bona fide hedging exemption within five business days after the trader assumed the position that exceeded a position limit.

(B) Must require, for any exemption granted, that the trader reapply for the exemption at least on an annual basis.

(C) May deny any such application, or limit, condition, or revoke any such exemption, at any time, including if it determines such positions would not be in accord with sound commercial practices, or would exceed an amount that may be established and liquidated in an orderly fashion.

(3) *Pre-enactment and transition period swap positions.* Speculative position limits set forth in § 150.2 shall not apply to positions acquired in good faith in any pre-enactment swap, or in any transition period swap, in either case as defined by § 150.1. *Provided however,* that a designated contract market or swap execution facility that is a trading facility shall allow a person to net such position with post-effective date commodity derivative contracts for the purpose of complying with any non-spot month speculative position limit.

(4) *Pre-existing positions*—(i) *Pre-existing positions in a spot-month.* A designated contract market or swap execution facility that is a trading facility must require compliance with spot month speculative position limits for pre-existing positions in commodity derivative contracts other than pre-enactment and transition period swaps.

(ii) *Pre-existing positions in a non-spot month.* A single-month or all months-combined speculative position limit established under § 150.2 shall not apply to any commodity derivative contract acquired in good faith prior to the effective date of such limit, *provided however,* that such position shall be attributed to the person if the person's position is increased after the effective date of such limit.

(5) *Aggregation.* Designated contract markets and swap execution facilities that are trading facilities must have aggregation rules that conform to § 150.4.

(6) *Additional acceptable practices.* A designated contract market or swap execution facility that is a trading facility may:

(i) Impose additional restrictions on a person with a long position in the spot month of a physical-delivery contract who stands for delivery, takes that delivery, then re-establishes a long position;

(ii) Establish limits on the amount of delivery instruments that a person may hold in a physical-delivery contract; and

(iii) Impose such other restrictions as it deems necessary to reduce the potential threat of market manipulation or congestion, to maintain orderly execution of transactions, or for such other purposes consistent with its responsibilities.

(b) *Requirements and acceptable practices for commodity derivative contracts in a physical commodity as defined in § 150.1 that are not subject to the limits set forth in § 150.2*—(1) *Levels at initial listing.* At the time of each commodity derivative contract's initial listing, a designated contract market or swap execution facility that is a trading facility should base speculative position limits on the following:

(i) *Spot month position limits*—(A) *Commodities with a measurable deliverable supply.* For all commodity derivative contracts not subject to the limits set forth in § 150.2 that are based on a commodity with a measurable deliverable supply, the spot month limit level should be established at a level that is no greater than one-quarter of the estimated spot month deliverable supply, calculated separately for each month to be listed (Designated Contract Markets and Swap Execution Facilities may refer to the guidance in paragraph (b)(1)(i) of Appendix C of part 38 of this chapter for guidance on estimating spot-month deliverable supply);

(B) *Commodities without a measurable deliverable supply.* For commodity derivative contracts that are based on a commodity with no measurable deliverable supply, the spot month limit level should be set at a level that is necessary and appropriate to reduce the potential threat of market manipulation or price distortion of the contract's or the underlying commodity's price or index.

(ii) *Individual non-spot or all-months combined position limits.* For agricultural or exempt commodity derivative contracts not subject to the limits set forth in § 150.2, the individual non-spot or all-months-combined levels should be equal to or less than the greater of: The level of the spot month limit; or 5,000 contracts, when the notional quantity per contract is no larger than a typical cash market transaction in the underlying commodity. If the notional quantity per contract is larger than the typical cash market transaction, then the individual non-spot month limit or all-months combined limit level should be scaled down accordingly. If the commodity derivative contract is substantially the same as a pre-existing commodity derivative contract, then the designated contract market or swap execution facility may adopt the same limit as applies to that pre-existing commodity derivative contract.

(iii) *Commodity derivative contracts that are cash-settled by referencing a daily settlement price of an existing contract.* For commodity derivative contracts that are cash-settled by referencing a daily settlement price of an existing contract listed on a designated contract market or swap execution facility that is a trading facility, the cash-settled contract should adopt spot-month, individual non-spot-month, and all-months combined position limits comparable to those of the original price referenced contract.

(2) *Adjustments to levels.* Designated contract markets and swap execution facilities that are trading facilities should adjust their speculative limit levels as follows:

(i) *Spot month position limits.* The spot month position limit level should be reviewed no less than once every twenty-four months from the date of initial listing and should be maintained at a level that is:

(A) No greater than one-quarter of the estimated spot month deliverable supply, calculated separately for each month to be listed; or

(B) In the case of a commodity derivative contract based on a commodity without a measurable deliverable supply, necessary and appropriate to reduce the potential threat of market manipulation or price distortion of the contract's or the underlying commodity's price or index.

(ii) *Individual non-spot or all-months-combined position limits.* Individual non-spot or all-months-combined levels should be based on position sizes customarily held by speculative traders on the contract market or equal to or less than the greater of: The spot-month position limit level; 10% of the average combined futures and delta adjusted option month-end open interest for the most recent calendar year up to 25,000 contracts, with a marginal increase of 2.5% thereafter; or 5,000 contracts. In any case, such levels should be reviewed no less than once every twenty-four months from the date of initial listing.

(3) *Position accountability in lieu of speculative position limits.* A designated contract market or swap execution facility that is a trading facility may adopt a bylaw, rule, regulation, or resolution, substituting for the exchange-set speculative position limits specified under this paragraph (b), an exchange rule requiring traders to consent to provide information about their position upon request by the exchange and to consent to halt increasing further a trader's position or to reduce their positions in an orderly manner, in each case upon request by the exchange as follows:

(i) *Physical commodity derivative contracts.* On a physical commodity derivative contract that is not subject to the limits set forth in § 150.2, having an average month-end open interest of 50,000 contracts and an average daily volume of 5,000 or more contracts during the most recent calendar year and a liquid cash market, a designated contract market or swap execution facility that is a trading facility may adopt individual non-spot month or all-months-combined position accountability levels, *provided however,* that such designated contract market or swap execution facility that is a trading facility should adopt a spot month speculative position limit with a level no greater than one-quarter of the estimated spot month deliverable supply.

(ii) *New commodity derivative contracts that are substantially the same as an existing contract.* On a new commodity derivative contract that is substantially the same as an existing commodity derivative contract listed for trading on a designated contract market or swap execution facility that is a trading facility, which has adopted position accountability in lieu of position limits, the designated contract market or swap execution facility may adopt for the new contract when it is initially listed for trading the position accountability levels of the existing contract.

(4) *Calculation of trading volume and open interest.* For purposes of this paragraph, trading volume and open interest should be calculated by:

(i) *Open interest.* (A) Averaging the month-end open positions in a futures contract and its related option contract, on a delta-adjusted basis, for all months listed during the most recent calendar year; and

(B) Averaging the month-end futures equivalent amount of open positions in swaps in a particular commodity (such as, for swaps that are not referenced contracts, by combining the notional month-end open positions in swaps in a particular commodity, including options in that same commodity that are swaps on a delta-adjusted basis, and dividing by a notional quantity per contract that is no larger than a typical cash market transaction in the underlying commodity), except that a designated contract market or swap execution facility that is a trading facility shall include swaps in their open interest calculation only if such entities administer position limits on swap contracts of their facilities.

(ii) *Trading volume.* (A) Counting the number of contracts in a futures contract and its related option contract, on a delta-adjusted basis, transacted during the most recent calendar year; and

(B) Counting the futures-equivalent number of swaps in a particular commodity transacted during the most recent calendar year, except that a designated contract market or swap execution facility that is a trading facility shall include swaps in their trading volume count only if such entities administer position limits on swap contracts of their facilities.

(5) *Exemptions*—(i) *Hedge exemption.* (A) Any hedge exemption rules adopted by a designated contract market or a swap execution facility that is a trading facility should conform to the definition of bona fide hedging position in § 150.1 and may provide for recognition as a non-enumerated bona fide hedge in a manner consistent with the process described in § 150.9(a).

(B) Any hedge exemption rules adopted under paragraph (b)(5)(i)(A) of this section may allow a person to file an application for enumerated hedging positions, which application should be filed not later than five business days after the person assumed the position that exceeded a position limit.

(ii) *Other exemptions.* A designated contract market or swap execution facility may grant other exemptions for:

(A) *Financial distress.* Upon specific request made to the designated contract market or swap execution facility that is a trading facility, the designated contract market or swap execution facility that is a trading facility may exempt a person or related persons under financial distress circumstances for a time certain from any of the requirements of this part. Financial distress circumstances include situations involving the potential default or bankruptcy of a customer of the requesting person or persons, an affiliate of the requesting person or persons, or a potential acquisition target of the requesting person or persons.

(B) *Conditional spot-month limit exemption.* Exchange-set spot-month speculative position limits may be exceeded for cash-settled contracts, *provided that* such positions should not exceed two times the level of the spot-month limit specified by the designated contract market or swap execution facility that is a trading facility, that lists a physical-delivery contract to which the cash-settled contracts are directly or indirectly linked, and the person holding or controlling such positions should not hold or control positions in such spot-month physical-delivery contract.

(C) *Intramarket spread positions and intermarket spread positions,* each as defined in § 150.1, *provided that* the designated contract market or swap execution facility, in considering whether to grant an application for such exemption, should take into account whether exempting the spread position from position limits would, to the maximum extent practicable, ensure sufficient market liquidity for bona fide hedgers, and not unduly reduce the effectiveness of position limits to:

(*1*) Diminish, eliminate, or prevent excessive speculation;

(*2*) Deter and prevent market manipulation, squeezes, and corners; and

(*3*) Ensure that the price discovery function of the underlying market is not disrupted.

(iii) *Application for exemption.* Traders should be required to apply to the designated contract market or swap execution facility that is a trading facility for any exemption from its speculative position limit rules. In considering whether to grant such an application for exemption, a designated contract market or swap execution facility that is a trading facility should take into account whether the requested exemption is in accord with sound commercial practices and results in a position that does not exceed an amount that may be established and liquidated in an orderly fashion.

(6) *Pre-enactment and transition period swap positions.* Speculative position limits should not apply to positions acquired in good faith in any pre-enactment swap, or in any transition period swap, in either case as defined by § 150.1. *Provided however,* that a designated contract market or swap execution facility that is a trading facility may allow a person to net such position with post-effective date commodity derivative contracts for the purpose of complying with any non-spot month speculative position limit.

(7) *Pre-existing positions*—(i) *Preexisting positions in a spot-month.* A designated contract market or swap execution facility that is a trading facility should require compliance with spot month speculative position limits for pre-existing positions in commodity derivative contracts other than pre-enactment and transition period swaps.

(ii) *Pre-existing positions in a non-spot month.* A single-month or all-months-combined speculative position limit should not apply to any commodity derivative contract acquired in good faith prior to the effective date of such limit, *provided however,* that such position should be attributed to the person if the person's position is increased after the effective date of such limit.

(8) *Aggregation.* Designated contract markets and swap execution facilities that are trading facilities must have aggregation rules that conform to § 150.4.

(9) *Additional acceptable practices.* Particularly in the spot month, a

designated contract market or swap execution facility that is a trading facility may:

(i) Impose additional restrictions on a person with a long position in the spot month of a physical-delivery contract who stands for delivery, takes that delivery, then re-establishes a long position;

(ii) Establish limits on the amount of delivery instruments that a person may hold in a physical-delivery contract; and

(iii) Impose such other restrictions as it deems necessary to reduce the potential threat of market manipulation or congestion, to maintain orderly execution of transactions, or for such other purposes consistent with its responsibilities.

(c) *Requirements and acceptable practices for excluded commodity derivative contracts as defined in section 1a(19) of the Act*—(1) *Levels at initial listing.* At the time of each excluded commodity derivative contract's initial listing, a designated contract market or swap execution facility that is a trading facility should base speculative position limits on the following:

(i) *Spot month position limits.*—(A) *Excluded commodity derivative contracts with a measurable deliverable supply.* For all excluded commodity derivative contracts that are based on a commodity with a measurable deliverable supply, the spot month limit level should be established at a level that is no greater than one-quarter of the estimated spot month deliverable supply, calculated separately for each month to be listed (Designated Contract Markets and Swap Execution Facilities may refer to the guidance in paragraph (b)(1)(i) of Appendix C of part 38 of this chapter for guidance on estimating spot-month deliverable supply);

(B) *Excluded commodity derivative contracts without a measurable deliverable supply.* For excluded commodity derivative contracts that are based on a commodity with no measurable deliverable supply, the spot month limit level should be set at a level that is necessary and appropriate to reduce the potential threat of market manipulation or price distortion of the contract's or the underlying commodity's price or index.

(ii) *Individual non-spot or all-months combined position limits.* For excluded commodity derivative contracts, the individual non-spot or all-months-combined levels should be equal to or less than the greater of: The level of the spot month limit; or 5,000 contracts, when the notional quantity per contract is no larger than a typical cash market transaction in the underlying commodity. If the notional quantity per contract is larger than the typical cash market transaction, then the individual non-spot month limit or all-months combined limit level should be scaled down accordingly. If the commodity derivative contract is substantially the same as a pre-existing commodity derivative contract, then the designated contract market or swap execution facility may adopt the same limit as applies to that pre-existing commodity derivative contract.

(iii) *Commodity derivative contracts that are cash-settled by referencing a daily settlement price of an existing contract.* For excluded commodity derivative contracts that are cash-settled by referencing a daily settlement price of an existing contract listed on a designated contract market or swap execution facility that is a trading facility, the cash-settled contract should adopt spot-month, individual non-spot-month, and all-months combined position limits that are comparable to those of the original price referenced contract.

(2) *Adjustments to levels.* Designated contract markets and swap execution facilities that are trading facilities should adjust their speculative limit levels as follows:

(i) *Spot month position limits.* The spot month position limit level for excluded commodity derivative contracts should be reviewed no less than once every twenty-four months from the date of initial listing and should be maintained at a level that is necessary and appropriate to reduce the potential threat of market manipulation or price distortion of the contract's or the underlying commodity's price or index.

(ii) *Individual non-spot or all-months-combined position limits.* Individual non-spot or all-months-combined levels should be based on position sizes customarily held by speculative traders on the contract market or equal to or less than the greater of: the spot-month position limit level; 10% of the average combined futures and delta adjusted option month-end open interest for the most recent calendar year up to 25,000 contracts, with a marginal increase of 2.5% thereafter; or 5,000 contracts. In any case, such levels should be reviewed no less than once every twenty-four months from the date of initial listing.

(3) *Position accountability in lieu of speculative position limits.* A designated contract market or swap execution facility that is a trading facility may adopt a bylaw, rule, regulation, or resolution, substituting for the exchange-set speculative position limits specified under this paragraph (c), an exchange rule requiring traders to consent to provide information about their position upon request by the exchange and to consent to halt increasing further a trader's position or to reduce their positions in an orderly manner, in each case upon request by the exchange as follows:

(i) *Spot month.* On an excluded commodity derivative contract for which there is a highly liquid cash market and no legal impediment to delivery, a designated contract market or swap execution facility that is a trading facility may adopt position accountability in lieu of position limits in the spot month. For an excluded commodity derivative contract based on a commodity without a measurable deliverable supply, a designated contract market or swap execution facility that is a trading facility may adopt position accountability in lieu of position limits in the spot month. For all other excluded commodity derivative contracts, a designated contract market or swap execution facility that is a trading facility should adopt a spot-month position limit with a level no greater than one-quarter of the estimated deliverable supply;

(ii) *Individual non-spot or all-months combined position limits.* On an excluded commodity derivative contract, a designated contract market or swap execution facility that is a trading facility may adopt position accountability levels in lieu of position limits in the individual non-spot month or all-months-combined.

(iii) *New commodity derivative contracts that are substantially the same as an existing contract.* On a new commodity derivative contract on an excluded commodity derivative contract that is substantially the same as an existing commodity derivative contract listed for trading on a designated contract market or swap execution facility that is a trading facility, which has adopted position accountability in lieu of position limits, the designated contract market or swap execution facility may adopt for the new contract when it is initially listed for trading the position accountability levels of the existing contract.

(4) *Calculation of trading volume and open interest.* For purposes of this paragraph, trading volume and open interest should be calculated by:

(i) *Open interest.* (A) Averaging the month-end open positions in a futures contract and its related option contract, on a delta-adjusted basis, for all months listed during the most recent calendar year; and

(B) Averaging the month-end futures equivalent amount of open positions in swaps in a particular commodity (such as, for swaps that are not referenced contracts, by combining the notional month-end open positions in swaps in a particular commodity, including options in that same commodity that are swaps on a delta-adjusted basis, and dividing by a notional quantity per contract that is no larger than a typical cash market transaction in the underlying commodity), except that a designated contract market or swap execution facility that is a trading facility should include swaps in their open interest calculation only if such entities administer position limits on swap contracts of their facilities.

(ii) *Trading volume.* (A) Counting the number of contracts in a futures contract and its related option contract, on a delta-adjusted basis, transacted during the most recent calendar year; and

(B) Counting the futures-equivalent number of swaps in a particular commodity transacted during the most recent calendar year, except that a designated contract market or swap execution facility that is a trading facility should include swaps in their trading volume count only if such entities administer position limits on swap contracts of their facilities.

(5) *Exemptions*—(i) *Hedge exemptions.* Any hedge exemption rules adopted by a designated contract market or a swap execution facility that is a trading facility should conform to the definition of bona fide hedging position in § 150.1.

(ii) *Other exemptions for excluded commodities.* A designated contract market or swap execution facility may grant, in addition to the exemptions under paragraphs (b)(5)(ii)(A), (b)(5)(ii)(B), and (b)(5)(ii)(C) of this section, a risk management exemption pursuant to rules submitted to the Commission, including for a position that is consistent with the guidance in Appendix A of this part.

(iii) *Application for exemption.* Traders should be required to apply to the designated contract market or swap execution facility that is a trading facility for any exemption from its speculative position limit rules. Such exchange may allow a person to file an application after the person assumed the position that exceeded a position limit. In considering whether to grant such an application for exemption, a designated contract market or swap execution facility that is a trading facility should take into account whether the requested exemption is in accord with sound commercial practices and results in a position that does not exceed an amount that may be established and liquidated in an orderly fashion.

(6) *Pre-enactment and transition period swap positions.* Speculative position limits should not apply to positions acquired in good faith in any pre-enactment swap, or in any transition period swap, in either case as defined by § 150.1. *Provided however,* that a designated contract market or swap execution facility that is a trading facility may allow a person to net such position with post-effective date commodity derivative contracts for the purpose of complying with any non-spot month speculative position limit.

(7) *Pre-existing positions*—(i) *Pre-existing positions in a spot-month.* A designated contract market or swap execution facility that is a trading facility should require compliance with spot month speculative position limits for pre-existing positions in commodity derivative contracts.

(ii) *Pre-existing positions in a non-spot month.* A single-month or all-months-combined speculative position limit should not apply to any commodity derivative contract acquired in good faith prior to the effective date of such limit, *provided however,* that such position should be attributed to the person if the person's position is increased after the effective date of such limit.

(8) *Aggregation.* Designated contract markets and swap execution facilities that are trading facilities should have aggregation rules for excluded commodity derivative contracts that conform to § 150.4.

(9) *Additional acceptable practices.* A designated contract market or swap execution facility that is a trading facility may impose such other restrictions on excluded commodity derivative contracts as it deems necessary to reduce the potential threat of market manipulation or congestion, to maintain orderly execution of transactions, or for such other purposes consistent with its responsibilities.

(d) *Requirements for security futures products.* For security futures products, position limitations and position accountability requirements are specified in § 41.25(a)(3) of this chapter.

■ 26. Revise § 150.6 to read as follows:

**§ 150.6 Ongoing application of the Act and Commission regulations.**

This part shall only be construed as having an effect on position limits set by the Commission or a designated contract market or swap execution facility, including any associated recordkeeping and reporting regulations. Nothing in this part shall be construed to affect any other provisions of the Act or Commission regulations, including but not limited to those relating to manipulation, attempted manipulation, corners, squeezes, fraudulent or deceptive conduct or prohibited transactions, unless incorporated by reference.

■ 27. Add §§ 150.7 through 150.11 to read as follows:

**§ 150.7 Requirements for anticipatory bona fide hedging position exemptions.**

(a) *Statement.* Any person who wishes to avail himself of exemptions for unfilled anticipated requirements, unsold anticipated production, anticipated royalties, anticipated services contract payments or receipts, or anticipatory cross-commodity hedges under the provisions of paragraphs (3)(iii), (4)(i), 4(iii), 4(iv), or (5), respectively, of the definition of bona fide hedging position in § 150.1 shall file an application on Form 704 with the Commission in advance of the date the person expects to exceed the position limits established under this part. Filings in conformity with the requirements of this section shall be effective ten days after submission, unless otherwise notified by the Commission.

(b) *Commission notification.* At any time, the Commission may, by notice to any person filing an application or annual update on Form 704, specify its determination as to what portion, if any, of the amounts described in such filing does not meet the requirements for bona fide hedging positions. In no case shall such person's anticipatory bona fide hedging positions exceed the levels specified in paragraph (f) of this section.

(c) *Call for additional information.* At any time, the Commission may request a person who has on file an application or annual update Form 704 under paragraph (a) of this section to file specific additional or updated information with the Commission to support a determination that the application or annual update on file accurately reflects unsold anticipated production, unfilled anticipated requirements, anticipated royalties, or anticipated services contract payments or receipts.

(d) *Initial statement and annual update.* Initial Form 704 concerning the classification of positions as bona fide hedging pursuant to paragraphs (3)(iii), or 4(i), 4(iii), 4(iv) or anticipatory cross-commodity hedges under paragraph (5) of the definition of bona fide hedging position in § 150.1 shall be filed with the Commission at least ten days in advance of the date that such positions would be in excess of limits then in effect pursuant to section 4a of the Act.

Each person that has filed an initial statement on Form 704 for an anticipatory bona fide hedge exemption shall provide annual updates on the utilization of the anticipatory exemption, including actual cash activity utilizing the anticipatory exemption for the preceding year, as well as the cumulative utilization since the filing of the initial or most recent annual statement. Such statements shall set forth in detail for a specified operating period the person's anticipated activity, *i.e.,* unfilled anticipated requirements, unsold anticipated production, anticipated royalties, or anticipated services contract payments or receipts, and explain the method of determination thereof, including, but not limited to, the following information:

(1) *For each anticipated activity:* (i) The type of cash commodity underlying the anticipated activity;

(ii) The name of the actual cash commodity underlying the anticipated activity and the units in which the cash commodity is measured;

(iii) An indication of whether the cash commodity is the same commodity (grade and quality) that underlies a core referenced futures contract or whether a cross-hedge will be used and, if so, additional information for cross hedges specified in paragraph (d)(2) of this section;

(iv)(A) Annual production, requirements, royalty receipts or service contract payments or receipts, in terms of futures equivalents, of such commodity for the three complete fiscal years preceding the current fiscal year, if filing an initial statement; or

(B) For the prior fiscal year if filing an annual update;

(v) The specified time period for which the anticipatory hedge exemption is claimed;

(vi) Anticipated production, requirements, royalty receipts or service contract payments or receipts, in terms of futures equivalents, of such commodity for such specified time period;

(vii) Fixed-price forward sales, inventory, and fixed-price forward purchases of such commodity, including any quantity in process of manufacture and finished goods and byproducts of manufacture or processing (in terms of such commodity);

(viii) Unsold anticipated production, unfilled anticipated requirements, unsold anticipated royalty receipts, and anticipated service contract payments or receipts the risks of which have not been offset with cash positions, of such commodity for the specified time period; and

(ix) The maximum number of long positions and short positions in referenced contracts expected to be used to offset the risks of such anticipated activity.

(2) *Additional information for cross hedges.* Cash positions that represent a commodity, or products or byproducts of a commodity, that is different from the commodity underlying a commodity derivative contract that is expected to be used for hedging, shall be shown both in terms of the equivalent amount of the commodity underlying the commodity derivative contract used for hedging and in terms of the actual cash commodity as provided for on Form 704. In computing their cash position, every person shall use such standards and conversion factors that are usual in the particular trade or that otherwise reflect the value-fluctuation-equivalents of the cash position in terms of the commodity underlying the commodity derivative contract used for hedging. Such person shall furnish to the Commission upon request detailed information concerning the basis for and derivation of such conversion factors, including:

(i) The hedge ratio used to convert the actual cash commodity to the equivalent amount of the commodity underlying the commodity derivative contract used for hedging; and

(ii) An explanation of the methodology used for determining the hedge ratio.

(e) *Monthly reporting.* Monthly reporting of remaining anticipated hedge exemption shall be reported on Form 204, along with reporting other exemptions pursuant to § 19.01(a)(3)(vii) of this chapter.

(f) *Maximum sales and purchases.* Sales or purchases of commodity derivative contracts considered to be bona fide hedging positions under paragraphs (3)(iii)(A) or (4)(i) of the bona fide hedging position definition in § 150.1 shall at no time exceed the lesser of:

(1) A person's anticipated activity (including production, requirements, royalties and services) as described by the information most recently filed pursuant to this section that has not been offset with cash positions; or

(2) Such lesser amount as determined by the Commission pursuant to paragraph (b) of this section.

(g) *Delegation of authority to the Director of the Division of Market Oversight.* (1) The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director may designate from time to time, the authority:

(i) In paragraph (b) of this section to provide notice to a person that some or all of the amounts described in a Form 704 filing does not meet the requirements for bona fide hedging positions;

(ii) In paragraph (c) of this section to request a person who has filed an application or annual update on Form 704 under paragraph (a) of this section to file specific additional or updated information with the Commission to support a determination that the Form 704 filed accurately reflects unsold anticipated production, unfilled anticipated requirements, anticipated royalties, or anticipated services contract payments or receipts; and

(iii) In paragraph (d)(2) of this section to request detailed information concerning the basis for and derivation of conversion factors used in computing the cash position provided in any applications or annual updates filed on Form 704.

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

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

**§ 150.8 Severability.**

If any provision of this part, or the application thereof to any person or circumstances, is held invalid, such invalidity shall not affect other provisions or application of such provision to other persons or circumstances which can be given effect without the invalid provision or application.

**§ 150.9 Process for recognition of positions as non-enumerated bona fide hedges.**

(a) *Requirements for a designated contract market or swap execution facility to recognize non-enumerated bona fide hedging positions.* (1) A designated contract market or swap execution facility that elects to process non-enumerated bona fide hedging position applications to demonstrate why a derivative position satisfies the requirements of section 4a(c) of the Act shall maintain rules, submitted to the Commission pursuant to part 40 of this chapter, establishing an application process for recognition of non-enumerated bona fide hedging positions consistent with the requirements of this section and the general definition of bona fide hedging position in § 150.1. A designated contract market or swap execution facility may elect to process non-enumerated bona fide hedging position applications for positions in commodity derivative contracts only if, in each case:

(i) The commodity derivative contract is a referenced contract;

(ii) Such designated contract market or swap execution facility lists such commodity derivative contract for trading;

(iii) Such commodity derivative contract is actively traded on such designated contract market or swap execution facility;

(iv) Such designated contract market or swap execution facility has established position limits for such commodity derivative contract; and

(v) Such designated contract market or swap execution facility has at least one year of experience and expertise administering position limits for a referenced contract in a particular commodity. A designated contract market or swap execution facility shall not recognize a non-enumerated bona fide hedging position involving a commodity index contract and one or more referenced contracts.

(2) A designated contract market or swap execution facility may establish different application processes for persons to demonstrate why a derivative position constitutes a non-enumerated bona fide hedging position under novel facts and circumstances and under facts and circumstances substantially similar to a position for which a summary has been published on such designated contract market's or swap execution facility's Web site, pursuant to paragraph (a)(7) of this section.

(3) Any application process that is established by a designated contract market or swap execution facility shall elicit sufficient information to allow the designated contract market or swap execution facility to determine, and the Commission to verify, whether the facts and circumstances in respect of a derivative position satisfy the requirements of section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1, and whether it is appropriate to recognize such position as a non-enumerated bona fide hedging position, including at a minimum:

(i) A description of the position in the commodity derivative contract for which the application is submitted and the offsetting cash positions;

(ii) Information to demonstrate why the position satisfies the requirements of section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1;

(iii) A statement concerning the maximum size of all gross positions in derivative contracts for which the application is submitted;

(iv) Information regarding the applicant's activity in the cash markets for the commodity underlying the position for which the application is submitted during the past year; and

(v) Any other information necessary to enable the designated contract market or swap execution facility to determine, and the Commission to verify, whether it is appropriate to recognize such position as a non-enumerated bona fide hedging position.

(4) Under any application process established under this section, a designated contract market or swap execution facility shall:

(i) Require each person intending to exceed position limits to submit an application, to reapply at least on an annual basis by updating that application, and to receive notice of recognition from the designated contract market or swap execution facility of a position as a non-enumerated bona fide hedging position in advance of the date that such position would be in excess of the limits then in effect pursuant to section 4a of the Act;

(ii) Notify an applicant in a timely manner if a submitted application is not complete. If an applicant does not amend or resubmit such application within a reasonable amount of time after such notice, a designated contract market or swap execution facility may reject the application;

(iii) Determine in a timely manner whether a derivative position for which a complete application has been submitted satisfies the requirements of section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1, and whether it is appropriate to recognize such position as a non-enumerated bona fide hedging position;

(iv) Have the authority to revoke, at any time, any recognition issued pursuant to this section if it determines the recognition is no longer in accord with section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1; and

(v) Notify an applicant in a timely manner:

(A) That the derivative position for which a complete application has been submitted has been recognized by the designated contract market or swap execution facility as a non-enumerated bona fide hedging position under this section, and the details and all conditions of such recognition;

(B) That its application is rejected, including the reasons for such rejection; or

(C) That the designated contract market or swap execution facility has asked the Commission to consider the application under paragraph (a)(8) of this section.

(5) An applicant's derivatives position shall be deemed to be recognized as a non-enumerated bona fide hedging position exempt from federal position limits at the time that a designated contract market or swap execution facility notifies an applicant that such designated contract market or swap execution facility will recognize such position as a non-enumerated bona fide hedging position.

(6) A designated contract market or swap execution facility that elects to process non-enumerated bona fide hedging position applications shall file new rules or rule amendments pursuant to part 40 of this chapter, establishing or amending requirements for an applicant to file reports pertaining to the use of any such exemption that has been granted in the manner, form, and frequency, as determined by the designated contract market or swap execution facility.

(7) After recognition of each unique type of derivative position as a non-enumerated bona fide hedging position, based on novel facts and circumstances, a designated contract market or swap execution facility shall publish on its Web site, on at least a quarterly basis, a summary describing the type of derivative position and explaining why it was recognized as a non-enumerated bona fide hedging position.

(8) If a non-enumerated bona fide hedging position application presents novel or complex issues or is potentially inconsistent with section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1, a designated contract market or swap execution facility may ask the Commission to consider the application under the process set forth in paragraph (d) of this section. The Commission may, in its discretion, agree to or reject any such request by a designated contract market or swap execution facility.

(b) *Recordkeeping.* (1) A designated contract market or swap execution facility that elects to process non-enumerated bona fide hedging position applications shall keep full, complete, and systematic records, which include all pertinent data and memoranda, of all activities relating to the processing of such applications and the disposition thereof, including the recognition by the designated contract market or swap execution facility of any derivative position as a non-enumerated bona fide hedging position, the revocation or modification of any such recognition, the rejection by the designated contract market or swap execution facility of an application, or the withdrawal, supplementation or updating of an application by the applicant. Included among such records shall be:

(i) All information and documents submitted by an applicant in connection with its application;

(ii) Records of oral and written communications between such designated contract market or swap execution facility and such applicant in connection with such application; and

(iii) All information and documents in connection with such designated contract market's or swap execution facility's analysis of and action on such application.

(2) All books and records required to be kept pursuant to this section shall be kept in accordance with the requirements of § 1.31 of this chapter.

(c) *Reports to the Commission.* (1) A designated contract market or swap execution facility that elects to process non-enumerated bona fide hedging position applications shall submit to the Commission a report for each week as of the close of business on Friday showing the following information:

(i) For each commodity derivative position that had been recognized that week by the designated contract market or swap execution facility as a non-enumerated bona fide hedging position, and for any revocation or modification of a previously granted recognition:

(A) The date of disposition,

(B) The effective date of the disposition,

(C) The expiration date of any recognition,

(D) Any unique identifier assigned by the designated contract market or swap execution facility to track the application,

(E) Any unique identifier assigned by the designated contract market or swap execution facility to a type of recognized non-enumerated bona fide hedging position,

(F) The identity of the applicant,

(G) The listed commodity derivative contract to which the application pertains,

(H) The underlying cash commodity,

(I) The maximum size of the commodity derivative position that is recognized by the designated contract market or swap execution facility as a non-enumerated bona fide hedging position,

(J) Any size limitation established for such commodity derivative position on the designated contract market or swap execution facility, and

(K) A concise summary of the applicant's activity in the cash markets for the commodity underlying the commodity derivative position; and

(ii) The summary of any non-enumerated bona fide hedging position published pursuant to paragraph (a)(7) of this section, or revised, since the last summary submitted to the Commission.

(2) Unless otherwise instructed by the Commission, a designated contract market or swap execution facility that elects to process non-enumerated bona fide hedging position applications shall submit to the Commission, no less frequently than monthly, any report such designated contract market or swap execution facility requires to be submitted by an applicant to such designated contract market or swap execution facility pursuant to rules required under paragraph (a)(6) of this section.

(3) Unless otherwise instructed by the Commission, a designated contract market or swap execution facility that elects to process non-enumerated bona fide hedging position applications shall submit to the Commission the information required by paragraphs (c)(1) and (2) of this section, as follows:

(i) As specified by the Commission on the Forms and Submissions page at *www.cftc.gov*;

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

(iii) Not later than 9:00 a.m. Eastern time on the third business day following the date of the report.

(d) *Review of applications by the Commission.* (1) The Commission may in its discretion at any time review any non-enumerated bona fide hedging position application submitted to a designated contract market or swap execution facility, and all records required to be kept by such designated contract market or swap execution facility pursuant to paragraph (b) of this section in connection with such application, for any purpose, including to evaluate whether the disposition of the application is consistent with section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1.

(i) The Commission may request from such designated contract market or swap execution facility records required to be kept by such designated contract market or swap execution facility pursuant to paragraph (b) of this section in connection with such application.

(ii) The Commission may request additional information in connection with such application from such designated contract market or swap execution facility or from the applicant.

(2) If the Commission preliminarily determines that any non-enumerated bona fide hedging position application or the disposition thereof by a designated contract market or swap execution facility presents novel or complex issues that require additional time to analyze, or that an application or the disposition thereof by such designated contract market or swap execution facility is potentially inconsistent with section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1, the Commission shall:

(i) Notify such designated contract market or swap execution facility and the applicable applicant of the issues identified by the Commission; and

(ii) Provide them with 10 business days in which to provide the Commission with any supplemental information.

(3) The Commission shall determine whether it is appropriate to recognize the derivative position for which such application has been submitted as a non-enumerated bona fide hedging position, or whether the disposition of such application by such designated contract market or swap execution facility is consistent with section 4a(c) the Act and the general definition of bona fide hedging position in § 150.1.

(4) If the Commission determines that the disposition of such application is inconsistent with section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1, the Commission shall notify the applicant and grant the applicant a commercially reasonable amount of time to liquidate the derivative position or otherwise come into compliance. This notification will briefly specify the nature of the issues raised and the specific provisions of the Act or the Commission's regulations with which the application is, or appears to be, inconsistent.

(e) *Review of summaries by the Commission.* The Commission may in its discretion at any time review any summary of a type of non-enumerated bona fide hedging position required to be published on a designated contract market's or swap execution facility's Web site pursuant to paragraph (a)(7) of this section for any purpose, including to evaluate whether the summary promotes transparency and fair and open access by all market participants to information regarding bona fide hedges. If the Commission determines that a summary is deficient in any way, the Commission shall notify such designated contract market or swap execution facility, and grant to the designated contract market or swap execution facility a reasonable amount of time to revise the summary.

(f) *Delegation of authority to the Director of the Division of Market Oversight.* (1) The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director may designate from time to time, the authority:

(i) In paragraph (a)(8) of this section to agree to or reject a request by a designated contract market or swap execution facility to consider a non-enumerated bona fide hedging position application;

(ii) In paragraph (c) of this section to provide instructions regarding the submission to the Commission of information required to be reported by a designated contract market or swap execution facility, to specify the manner for submitting such information on the Forms and Submissions page at *www.cftc.gov*, and to determine the format, coding structure, and electronic data transmission procedures for submitting such information;

(iii) In paragraph (d)(1) of this section to review any non-enumerated bona fide hedging position application and all records required to be kept by a designated contract market or swap execution facility in connection with such application, to request such records from such designated contract market or swap execution facility, and to request additional information in connection with such application from such designated contract market or swap execution facility or from the applicant;

(iv) In paragraph (d)(2) of this section to preliminarily determine that a non-enumerated bona fide hedging position application or the disposition thereof by a designated contract market or swap execution facility presents novel or complex issues that require additional time to analyze, or that such application or the disposition thereof is potentially inconsistent with section 4a(c) of the Act and the general definition of bona fide hedging position in § 150.1, to notify the designated contract market or swap execution facility and the applicable applicant of the issues identified, and to provide them with 10 business days in which to file supplemental information; and

(v) In paragraph (e) of this section to review any summary of a type of non-enumerated bona fide hedging position required to be published on a designated contract market's or swap execution facility's Web site, to determine that any such summary is deficient, to notify a designated contract market or swap execution facility of a deficient summary, and to grant such designated contract market or swap execution facility a reasonable amount of time to revise such summary.

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

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

**§ 150.10 Process for designated contract market or swap execution facility exemption from position limits for certain spread positions.**

(a) *Requirements for a designated contract market or swap execution facility to exempt from position limits certain positions normally known to the trade as spreads.* (1) A designated contract market or swap execution facility that elects to process applications for exemptions from position limits for certain positions normally known to the trade as spreads shall maintain rules, submitted to the Commission pursuant to part 40 of this chapter, establishing an application process for exempting positions normally known to the trade as spreads consistent with the requirements of this section. A designated contract market or swap execution facility may elect to process applications for such spread exemptions only if, in each case:

(i) Such designated contract market or swap execution facility lists for trading at least one contract that is either a component of the spread or a referenced contract that is a component of the spread;

(ii) The contract, in paragraph (a)(1)(i) of this section, in a particular commodity is actively traded on such designated contract market or swap execution facility;

(iii) Such designated contract market or swap execution facility has established position limits for at least one contract that is either a component of the spread or a referenced contract that is a component of the spread; and

(iv) Such designated contract market or swap execution facility has at least one year of experience and expertise administering position limits for at least one contract that is either a component of the spread or a referenced contract that is a component of the spread. A designated contract market or swap execution facility shall not approve a spread exemption involving a commodity index contract and one or more referenced contracts.

(2) Spreads that a designated contract market or swap execution facility may approve under this section include:

(i) Calendar spreads;

(ii) Quality differential spreads;

(iii) Processing spreads; and

(iv) Product or by-product differential spreads.

(3) Any application process that is established by a designated contract market or swap execution facility under this section shall elicit sufficient information to allow the designated contract market or swap execution facility to determine, and the Commission to verify, whether the facts and circumstances demonstrate that it is appropriate to exempt a spread position from position limits, including at a minimum:

(i) A description of the spread position for which the application is submitted;

(ii) Information to demonstrate why the spread position should be exempted from position limits, including how the exemption would further the purposes of section 4a(a)(3)(B) of the Act;

(iii) A statement concerning the maximum size of all gross positions in derivative contracts for which the application is submitted; and

(iv) Any other information necessary to enable the designated contract market or swap execution facility to determine, and the Commission to verify, whether it is appropriate to exempt such spread position from position limits.

(4) Under any application process established under this section, a designated contract market or swap execution facility shall:

(i) Require each person requesting an exemption from position limits for its spread position to submit an application, to reapply at least on an annual basis by updating that application, and to receive approval in advance of the date that such position would be in excess of the limits then in effect pursuant to section 4a of the Act;

(ii) Notify an applicant in a timely manner if a submitted application is not complete. If an applicant does not amend or resubmit such application within a reasonable amount of time after such notice, a designated contract market or swap execution facility may reject the application;

(iii) Determine in a timely manner whether a spread position for which a complete application has been submitted satisfies the requirements of paragraph (a)(4)(vi) of this section, and whether it is appropriate to exempt such spread position from position limits;

(iv) Have the authority to revoke, at any time, any spread exemption issued pursuant to this section if it determines the spread exemption no longer satisfies the requirements of paragraph (a)(4)(vi) of this section and it is no longer appropriate to exempt the spread from position limits;

(v) Notify an applicant in a timely manner:

(A) That a spread position for which a complete application has been submitted has been exempted by the designated contract market or swap execution facility from position limits, and the details and all conditions of such exemption;

(B) That its application is rejected, including the reasons for such rejection; or

(C) That the designated contract market or swap execution facility has asked the Commission to consider the application under paragraph (a)(8) of this section; and

(vi) Determine whether exempting the spread position from position limits would, to the maximum extent practicable, ensure sufficient market liquidity for bona fide hedgers, and not unreasonably reduce the effectiveness of position limits to:

(A) Diminish, eliminate or prevent excessive speculation;

(B) Deter and prevent market manipulation, squeezes, and corners; and

(C) Ensure that the price discovery function of the underlying market is not disrupted.

(5) An applicant's derivatives position shall be deemed to be recognized as a spread position exempt from federal position limits at the time that a designated contract market or swap execution facility notifies an applicant that such designated contract market or swap execution facility will exempt such spread position.

(6) A designated contract market or swap execution facility that elects to process applications to exempt spread positions from position limits shall file new rules or rule amendments pursuant to part 40 of this chapter, establishing or amending requirements for an applicant to file reports pertaining to the use of any such exemption that has been granted in the manner, form, and frequency, as determined by the designated contract market or swap execution facility.

(7) After exemption of each unique type of spread position, a designated contract market or swap execution facility shall publish on its Web site, on at least a quarterly basis, a summary describing the type of spread position and explaining why it was exempted.

(8) If a spread exemption application presents complex issues or is potentially inconsistent with the purposes of section 4a(a)(3)(B) of the Act, a designated contract market or swap execution facility may ask the Commission to consider the application under the process set forth in paragraph (d) of this section. The Commission may, in its discretion, agree to or reject any such request by a designated contract market or swap execution facility.

(b) *Recordkeeping.* (1) A designated contract market or swap execution facility that elects to process spread exemption applications shall keep full, complete, and systematic records, which include all pertinent data and memoranda, of all activities relating to the processing of such applications and the disposition thereof, including the exemption of any spread position, the revocation or modification of any exemption, the rejection by the designated contract market or swap execution facility of an application, or the withdrawal, supplementation or updating of an application by the applicant. Included among such records shall be:

(i) All information and documents submitted by an applicant in connection with its application;

(ii) Records of oral and written communications between such designated contract market or swap execution facility and such applicant in connection with such application; and

(iii) All information and documents in connection with such designated contract market's or swap execution facility's analysis of and action on such application.

(2) All books and records required to be kept pursuant to this section shall be kept in accordance with the requirements of § 1.31 of this chapter.

(c) *Reports to the Commission.* (1) A designated contract market or swap execution facility that elects to process spread exemption applications shall submit to the Commission a report for each week as of the close of business on Friday showing the following information:

(i) The disposition of any spread exemption application, including the exemption of any spread position, the revocation or modification of any exemption, or the rejection of any application, as well as the following details:

(A) The date of disposition,

(B) The effective date of the disposition,

(C) The expiration date of any exemption,

(D) Any unique identifier assigned by the designated contract market or swap execution facility to track the application,

(E) Any unique identifier assigned by the designated contract market or swap execution facility to a type of exempt spread position,

(F) The identity of the applicant,

(G) The listed commodity derivative contract to which the application pertains,

(H) The underlying cash commodity,

(I) The size limitations on any exempt spread position, specified by contract month if applicable, and

(J) Any conditions on the exemption; and

(ii) The summary of any exempt spread position newly published pursuant to paragraph (a)(7) of this section, or revised, since the last summary submitted to the Commission.

(2) Unless otherwise instructed by the Commission, a designated contract market or swap execution facility that elects to process applications to exempt spread positions from position limits shall submit to the Commission, no less frequently than monthly, any report such designated contract market or swap execution facility requires to be submitted by an applicant to such designated contract market or swap execution facility pursuant to rules required by paragraph (a)(6) of this section.

(3) Unless otherwise instructed by the Commission, a designated contract market or swap execution facility that elects to process applications to exempt spread positions from position limits shall submit to the Commission the information required by paragraphs (c)(1) and (2) of this section, as follows:

(i) As specified by the Commission on the Forms and Submissions page at *www.cftc.gov*;

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

(iii) Not later than 9:00 a.m. Eastern time on the third business day following the date of the report.

(d) *Review of applications by the Commission.* (1) The Commission may in its discretion at any time review any spread exemption application submitted to a designated contract market or swap execution facility, and all records required to be kept by such designated contract market or swap execution facility pursuant to paragraph (b) of this section in connection with such application, for any purpose, including to evaluate whether the disposition of the application is consistent with the purposes of section 4a(a)(3)(B) of the Act.

(i) The Commission may request from such designated contract market or swap execution facility records required to be kept by such designated contract market or swap execution facility pursuant to paragraph (b) of this section in connection with such application.

(ii) The Commission may request additional information in connection with such application from such designated contract market or swap execution facility or from the applicant.

(2) If the Commission preliminarily determines that any application to exempt a spread position from position limits, or the disposition thereof by a designated contract market or swap execution facility, presents novel or complex issues that require additional time to analyze, or that an application or the disposition thereof by such designated contract market or swap execution facility is potentially inconsistent with the Act, the Commission shall:

(i) Notify such designated contract market or swap execution facility and the applicable applicant of the issues identified by the Commission; and

(ii) Provide them with 10 business days in which to provide the Commission with any supplemental information.

(3) The Commission shall determine whether it is appropriate to exempt the spread position for which such application has been submitted from position limits, or whether the disposition of such application by such designated contract market or swap execution facility is consistent with the purposes of section 4a(a)(3)(B) of the Act.

(4) If the Commission determines that it is not appropriate to exempt the spread position for which such application has been submitted from position limits, or that the disposition of such application is inconsistent with the Act, the Commission shall notify the applicant and grant the applicant a commercially reasonable amount of time to liquidate the spread position or otherwise come into compliance. This notification will briefly specify the nature of the issues raised and the specific provisions of the Act or the Commission's regulations with which the application is, or appears to be, inconsistent.

(e) *Review of summaries by the Commission.* The Commission may in its discretion at any time review any summary of a type of spread position required to be published on a designated contract market's or swap execution facility's Web site pursuant to paragraph (a)(7) of this section for any purpose, including to evaluate whether the summary promotes transparency and fair and open access by all market participants to information regarding spread exemptions. If the Commission determines that a summary is deficient in any way, the Commission shall notify such designated contract market or swap execution facility, and grant to the designated contract market or swap execution facility a reasonable amount of time to revise the summary.

(f) *Delegation of authority to the Director of the Division of Market Oversight.* (1) The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director may designate from time to time, the authority:

(i) In paragraph (a)(8) of this section to agree to or reject a request by a designated contract market or swap execution facility to consider a spread exemption application;

(ii) In paragraph (c) of this section to provide instructions regarding the submission to the Commission of information required to be reported by a designated contract market or swap execution facility, to specify the manner for submitting such information on the Forms and Submissions page at *www.cftc.gov*, and to determine the format, coding structure, and electronic data transmission procedures for submitting such information;

(iii) In paragraph (d)(1) of this section to review any spread exemption application and all records required to be kept by a designated contract market or swap execution facility in connection with such application, to request such records from such designated contract market or swap execution facility, and to request additional information in connection with such application from such designated contract market or swap execution facility, or from the applicant;

(iv) In paragraph (d)(2) of this section to preliminarily determine that a spread exemption application or the disposition thereof by a designated contract market or swap execution facility presents complex issues that require additional time to analyze, or that such application or the disposition thereof is potentially inconsistent with the Act, to notify the designated contract market or swap execution facility and the applicable applicant of the issues identified, and to provide them with 10 business days in which to file supplemental information; and

(v) In paragraph (e) of this section to review any summary of a type of spread exemption required to be published on a designated contract market's or swap execution facility's Web site, to determine that any such summary is deficient, to notify a designated contract market or swap execution facility of a deficient summary, and to grant such designated contract market or swap execution facility a reasonable amount of time to revise such summary.

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

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

**§ 150.11 Process for recognition of positions as bona fide hedges for unfilled anticipated requirements, unsold anticipated production, anticipated royalties, anticipated service contract payments or receipts, or anticipatory cross-commodity hedge positions.**

(a) *Requirements for a designated contract market or swap execution facility to recognize certain enumerated anticipatory bona fide hedging positions.* (1) A designated contract market or swap execution facility that elects to process applications for recognition of positions as hedges of unfilled anticipated requirements, unsold anticipated production, anticipated royalties, anticipated service contract payments or receipts, or anticipatory cross-commodity hedges under the provisions of paragraphs (3)(iii), (4)(i), (iii), (iv), or (5), respectively, of the definition of bona fide hedging position in § 150.1 shall maintain rules, submitted to the Commission pursuant to part 40 of this chapter, establishing an application process for such anticipatory bona fide hedges consistent with the requirements of this section. A designated contract market or swap execution facility may elect to process such anticipatory hedge applications for positions in commodity derivative contracts only if, in each case:

(i) The commodity derivative contract is a referenced contract;

(ii) Such designated contract market or swap execution facility lists such commodity derivative contract for trading;

(iii) Such commodity derivative contract is actively traded on such derivative contract market;

(iv) Such designated contract market or swap execution facility has established position limits for such commodity derivative contract; and

(v) Such designated contract market or swap execution facility has at least one year of experience and expertise administering position limits for a referenced contract in a particular commodity.

(2) Any application process that is established by a designated contract

market or swap execution facility shall require, at a minimum, the information required under § 150.7(d).

(3) Under any application process established under this section, a designated contract market or swap execution facility shall:

(i) Require each person intending to exceed position limits to submit an application, and to reapply at least on an annual basis by updating that application, as required under § 150.7(d), and to receive notice of recognition from the designated contract market or swap execution facility of a position as a bona fide hedging position in advance of the date that such position would be in excess of the limits then in effect pursuant to section 4a of the Act;

(ii) Notify an applicant in a timely manner if a submitted application is not complete. If the applicant does not amend or resubmit such application within a reasonable amount of time after notification from the designated contract market or swap execution facility, the designated contract market or swap execution facility may reject the application;

(iii) Inform an applicant within ten days of receipt of such application by the designated contract market or swap execution facility that:

(A) The derivative position for which a complete application has been submitted has been recognized by the designated contract market or swap execution facility as a bona fide hedging position, and the details and all conditions of such recognition;

(B) The application is rejected, including the reasons for such rejection; or

(C) The designated contract market or swap execution facility has asked the Commission to consider the application under paragraph (a)(6) of this section; and

(iv) Have the authority to revoke, at any time, any recognition issued pursuant to this section if it determines the position no longer complies with the filing requirements under paragraph (a)(2) of this section.

(4) An applicant's derivatives position shall be deemed to be recognized as a bona fide hedging position at the time that a designated contract market or swap execution facility notifies an applicant that such designated contract market or swap execution facility will recognize such position as a bona fide hedging position.

(5) A designated contract market or swap execution facility that elects to process bona fide hedging position applications shall file new rules or rule amendments pursuant to part 40 of this chapter, establishing or amending requirements for an applicant to file the supplemental reports, as required under § 150.7(e), pertaining to the use of any such exemption that has been granted.

(6) A designated contract market or swap execution facility may ask the Commission to consider any application made under this section. The Commission may, in its discretion, agree to or reject any such request by a designated contract market or swap execution facility, *provided that,* if the Commission agrees to the request, it will have 10 business days from the time of the request to carry out its review.

(b) *Recordkeeping.* (1) A designated contract market or swap execution facility that elects to process bona fide hedging position applications under this section shall keep full, complete, and systematic records, which include all pertinent data and memoranda, of all activities relating to the processing of such applications and the disposition thereof, including the recognition of any derivative position as a bona fide hedging position, the revocation or modification of any recognition, the rejection by the designated contract market or swap execution facility of an application, or withdrawal, supplementation or updating of an application. Included among such records shall be:

(i) All information and documents submitted by an applicant in connection with its application;

(ii) Records of oral and written communications between such designated contract market or swap execution facility and such applicant in connection with such application; and

(iii) All information and documents in connection with such designated contract market's or swap execution facility's analysis of and action on such application.

(2) All books and records required to be kept pursuant to this section shall be kept in accordance with the requirements of § 1.31 of this chapter.

(c) *Reports to the Commission.* (1) A designated contract market or swap execution facility that elects to process bona fide hedging position applications under this section shall submit to the Commission a report for each week as of the close of business on Friday showing the following information:

(i) The disposition of any application, including the recognition of any position as a bona fide hedging position, the revocation or modification of any recognition, as well as the following details:

(A) The date of disposition,

(B) The effective date of the disposition,

(C) The expiration date of any recognition,

(D) Any unique identifier assigned by the designated contract market or swap execution facility to track the application,

(E) Any unique identifier assigned by the designated contract market or swap execution facility to a bona fide hedge recognized under this section;

(F) The identity of the applicant,

(G) The listed commodity derivative contract to which the application pertains,

(H) The underlying cash commodity,

(I) The maximum size of the commodity derivative position that is recognized by the designated contract market or swap execution facility as a bona fide hedging position,

(J) Any size limitation established for such commodity derivative position on the designated contract market or swap execution facility, and

(K) A concise summary of the applicant's activity in the cash market for the commodity underlying the position for which the application was submitted.

(2) Unless otherwise instructed by the Commission, a designated contract market or swap execution facility that elects to process bona fide hedging position applications shall submit to the Commission the information required by paragraph (c)(1) of this section, as follows:

(i) As specified by the Commission on the Forms and Submissions page at *www.cftc.gov*;

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

(iii) Not later than 9:00 a.m. Eastern time on the third business day following the date of the report.

(d) *Review of applications by the Commission.* (1) The Commission may in its discretion at any time review any bona fide hedging position application submitted to a designated contract market or swap execution facility under this section, and all records required to be kept by such designated contract market or swap execution facility pursuant to paragraph (b) of this section in connection with such application, for any purpose, including to evaluate whether the disposition of the application is consistent with the Act.

(i) The Commission may request from such designated contract market or swap execution facility records required to be kept by such designated contract market or swap execution facility pursuant to paragraph (b) of this section in connection with such application.

(ii) The Commission may request additional information in connection with such application from such designated contract market or swap execution facility or from the applicant.

(2) If the Commission preliminarily determines that any anticipatory hedge application is inconsistent with the filing requirements of § 150.11(a)(2), the Commission shall:

(i) Notify such designated contract market or swap execution facility and the applicable applicant of the deficiencies identified by the Commission; and

(ii) Provide them with 10 business days in which to provide the Commission with any supplemental information.

(3) If the Commission determines that the anticipatory hedge application is inconsistent with the filing requirements of § 150.11(a)(2), the Commission shall notify the applicant and grant the applicant a commercially reasonable amount of time to liquidate the derivative position or otherwise come into compliance. This notification will briefly specify the specific provisions of the filing requirements of § 150.11(a)(2), with which the application is, or appears to be, inconsistent.

(e) *Delegation of authority to the Director of the Division of Market Oversight.* (1) The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as the Director may designate from time to time, the authority:

(i) In paragraph (a)(6) of this section to agree to or reject a request by a designated contract market or swap execution facility to consider a bona fide hedge application;

(ii) In paragraph (c) of this section to provide instructions regarding the submission to the Commission of information required to be reported by a designated contract market or swap execution facility, to specify the manner for submitting such information on the Forms and Submissions page at *www.cftc.gov*, and to determine the format, coding structure, and electronic data transmission procedures for submitting such information;

(iii) In paragraph (d)(1) of this section to review any bona fide hedging position application and all records required to be kept by a designated contract market or swap execution facility in connection with such application, to request such records from such designated contract market or swap execution facility, and to request additional information in connection with such application from such designated contract market or swap execution facility or from the applicant; and

(iv) In paragraph (d)(2) of this section to determine that it is not appropriate to recognize a derivative position for which an application for recognition has been submitted as a bona fide hedging position, or that the disposition of such application by a designated contract market or swap execution facility is inconsistent with the Act, and, in connection with such a determination, to grant the applicant a reasonable amount of time to liquidate the derivative position or otherwise come into compliance.

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

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

■ 28. In Part 150, add Appendices A through E to read as follows:

## Appendix A to Part 150—Guidance on Risk Management Exemptions for Commodity Derivative Contracts in Excluded Commodities

(1) This appendix provides non-exclusive interpretative guidance on risk management exemptions for commodity derivative contracts in excluded commodities permitted under the definition of bona fide hedging position in § 150.1. The rules of a designated contract market or swap execution facility that is a trading facility may recognize positions consistent with this guidance as bona fide hedging positions. The Commission recognizes that risk management positions in commodity derivative contracts in excluded commodities may not conform to the general definition of bona fide hedging positions applicable to commodity derivative contracts in physical commodities, as provided under section 4a(c)(2) of the Act, and may not conform to enumerated bona fide hedging positions applicable to commodity derivative contracts in physical commodities under the definition of bona fide hedging position in § 150.1.

This interpretative guidance for core principle 5 for designated contract markets, section 5(d)(5) of the Act, and core principle 6 for swap execution facilities that are trading facilities, section 5h(f)(6) of the Act, is illustrative only of the types of positions for which a trading facility may elect to provide a risk management exemption and is not intended to be used as a mandatory checklist. Other positions might also be included appropriately within a risk management exemption.

(2)(a) *No temporary substitute criterion.* Risk management positions in commodity derivative contracts in excluded commodities need not be expected to represent a substitute for a subsequent transaction or position in a physical marketing channel. There need not be any requirement to replace a commodity derivative contract with a cash market position in order to qualify for a risk management exemption.

(b) *Cross-commodity hedging is permitted.* Risks that are offset in commodity derivative contracts in excluded commodities need not arise from the same commodities underlying the commodity derivative contracts. For example, a trading facility may recognize a risk management exemption based on the net interest rate risk arising from a bank's balance sheet of loans and deposits that is offset using Treasury security futures contracts or short-term interest rate futures contracts.

(3) *Examples of risk management positions.* This section contains examples of risk management positions that may be appropriate for management of risk in the operation of a commercial enterprise.

(a) *Balance sheet hedging.* A commercial enterprise may have risks arising from its net position in assets and liabilities.

(i) *Foreign currency translation.* One form of balance sheet hedging involves offsetting net exposure to changes in currency exchange rates for the purpose of stabilizing the domestic dollar accounting value of net assets and/or liabilities which are denominated in a foreign currency. For example, a bank may make loans in a foreign currency and take deposits in that same foreign currency. Such a bank is exposed to net foreign currency translation risk when the amount of loans is not equal to the amount of deposits. A bank with a net long exposure to a foreign currency may hedge by establishing an offsetting short position in a foreign currency commodity derivative contract.

(ii) *Interest rate risk.* Another form of balance sheet hedging involves offsetting net exposure to changes in values of assets and liabilities of differing durations. Examples include:

(A) A pension fund may invest in short term securities and have longer term liabilities. Such a pension fund has a duration mismatch. Such a pension fund may hedge by establishing a long position in Treasury security futures contracts to lengthen the duration of its assets to match the duration of its liabilities. This is economically equivalent to using a long position in Treasury security futures contracts to shorten the duration of its liabilities to match the duration of its assets.

(B) A bank may make a certain amount of fixed-rate loans of one maturity and fund such assets through taking fixed-rate deposits of a shorter maturity. Such a bank is exposed to interest rate risk, in that an increase in interest rates may result in a greater decline in value of the assets than the decline in value of the deposit liabilities. A bank may hedge by establishing a short position in short-term interest rate futures contracts to lengthen the duration of its liabilities to match the duration of its assets. This is economically equivalent to using a short position in short-term interest rate futures contracts, for example, to shorten the duration of its assets to match the duration of its liabilities.

(b) *Unleveraged synthetic positions.* An investment fund may have risks arising from a delayed investment in an asset allocation promised to investors. Such a fund may synthetically gain exposure to an asset class using a risk management strategy of establishing a long position in commodity derivative contracts that does not exceed cash set aside in an identifiable manner, including short-term investments, any funds deposited as margin and accrued profits on such commodity derivative contract positions. For example:

(i) A collective investment fund that invests funds in stocks pursuant to an asset allocation strategy may obtain immediate stock market exposure upon receipt of new monies by establishing a long position in stock index futures contracts (''equitizing cash''). Such a long position may qualify as a risk management exemption under trading facility rules provided such long position does not exceed the cash set aside. The long position in stock index futures contracts need not be converted to a position in stock.

(ii) Upon receipt of new funds from investors, an insurance company that invests in bond holdings for a separate account wishes to lengthen synthetically the duration of the portfolio by establishing a long position in Treasury futures contracts. Such a long position may qualify as a risk management exemption under trading facility rules provided such long position does not exceed the cash set aside. The long position in Treasury futures contracts need not be converted to a position in bonds.

(c) *Temporary asset allocations.* A commercial enterprise may have risks arising from potential transactional costs in temporary asset allocations (altering portfolio exposure to certain asset classes such as equity securities and debt securities). Such an enterprise may hedge existing assets owned by establishing a short position in an appropriate commodity derivative contract and synthetically gain exposure to an alternative asset class using a risk management strategy of establishing a long position in another commodity derivative contract that does not exceed: the value of the existing asset at the time the temporary asset allocation is established or, in the alternative, the hedged value of the existing asset plus any accrued profits on such risk management positions. For example:

(i) A collective investment fund that invests funds in bonds and stocks pursuant to an asset allocation strategy may believe that market considerations favor a temporary increase in the fund's equity exposure relative to its bond holdings. The fund manager may choose to accomplish the reallocation using commodity derivative contracts, such as a short position in Treasury security futures contracts and a long position in stock index futures contracts. The short position in Treasury security futures contracts may qualify as a hedge of interest rate risk arising from the bond holdings. A trading facility may adopt rules to recognize as a risk management exemption such a long position in stock index futures.

(ii) Reserved.

(4) *Clarification of bona fides of short positions.*

(a) *Calls sold.* A seller of a call option establishes a short call option. A short call option is a short position in a commodity derivative contract with respect to the underlying commodity. A bona fide hedging position includes such a written call option that does not exceed in quantity the ownership or fixed-price purchase contracts in the contract's underlying cash commodity by the same person.

(b) *Puts purchased and portfolio insurance.* A buyer of a put option establishes a long put option. However, a long put option is a short position in a commodity derivative contract with respect to the underlying commodity. A bona fide hedging position includes such an owned put that does not exceed in quantity the ownership or fixed-price purchase contracts in the contract's underlying cash commodity by the same person.

The Commission also recognizes as bona fide hedging positions strategies that provide protection against a price decline equivalent to an owned position in a put option for an existing portfolio of securities owned. A dynamically managed short position in a futures contract may replicate the characteristics of a long position in a put option.

(c) *Synthetic short futures contracts.* A person may establish a synthetic short futures position by purchasing a put option and selling a call option, when each option has the same notional amount, strike price, expiration date and underlying commodity. Such a synthetic short futures position is a short position in a commodity derivative contract with respect to the underlying commodity. A bona fide hedging position includes such a synthetic short futures position that does not exceed in quantity the ownership or fixed-price purchase contracts in the contract's underlying cash commodity by the same person.

## Appendix B to Part 150—Commodities Listed as Substantially the Same for Purposes of the Definition of Location Basis Contract

The following table lists core referenced futures contracts and commodities that are treated as substantially the same as a commodity underlying a core referenced futures contract for purposes of the definition of location basis contract in § 150.1.

LOCATION BASIS CONTRACT LIST OF SUBSTANTIALLY THE SAME COMMODITIES

| Core referenced futures contract | Commodities considered substantially the same (regardless of location) | Source(s) for specification of quality |
|---|---|---|
| NYMEX Light Sweet Crude Oil futures contract (CL) | 1. Light Louisiana Sweet (LLS) Crude Oil | NYMEX Argus LLS vs. WTI (Argus) Trade Month futures contract (E5).<br>NYMEX LLS (Argus) vs. WTI Financial futures contract (WJ).<br>ICE Futures Europe Crude Diff—Argus LLS vs WTI 1st Line Swap futures contract (ARK).<br>ICE Futures Europe Crude Diff—Argus LLS vs WTI Trade Month Swap futures contract (ARL). |
| NYMEX New York Harbor ULSD Heating Oil futures contract (HO) | 1. Chicago ULSD | NYMEX Chicago ULSD (Platts) vs. NY Harbor ULSD Heating Oil futures contract (5C). |
| | 2. Gulf Coast ULSD | NYMEX Group Three ULSD (Platts) vs. NY Harbor ULSD Heating Oil futures contract (A6).<br>NYMEX Gulf Coast ULSD (Argus) Up-Down futures contract (US).<br>NYMEX Gulf Coast ULSD (Argus) Up-Down BALMO futures contract (GUD).<br>NYMEX Gulf Coast ULSD (Platts) Up-Down BALMO futures contract (1L).<br>NYMEX Gulf Coast ULSD (Platts) Up-Down Spread futures contract (LT). |

LOCATION BASIS CONTRACT LIST OF SUBSTANTIALLY THE SAME COMMODITIES—Continued

| Core referenced futures contract | Commodities considered substantially the same (regardless of location) | Source(s) for specification of quality |
|---|---|---|
| | | ICE Futures Europe Diesel Diff—Gulf Coast vs Heating Oil 1st Line Swap futures contract (GOH).<br>CME Clearing Europe Gulf Coast ULSD( Platts) vs. New York Heating Oil (NYMEX) Spread Calendar swap (ELT).<br>CME Clearing Europe New York Heating Oil (NYMEX) vs. European Gasoil (IC) Spread Calendar swap (EHA). |
| | 3. California Air Resources Board Spec ULSD (CARB no. 2 oil). | NYMEX Los Angeles CARB Diesel (OPIS) vs. NY Harbor ULSD Heating Oil futures contract (KL). |
| | 4. Gas Oil Deliverable in Antwerp, Rotterdam, or Amsterdam Area. | ICE Futures Europe Gasoil futures contract (G).<br>ICE Futures Europe Heating Oil Arb—Heating Oil 1st Line vs Gasoil 1st Line Swap futures contract (HOT).<br>ICE Futures Europe Heating Oil Arb—Heating Oil 1st Line vs Low Sulphur Gasoil 1st Line Swap futures contract (ULL).<br>NYMEX NY Harbor ULSD Heating Oil vs. Gasoil futures contract (HA). |
| NYMEX RBOB Gasoline futures contract (RB) | 1. Chicago Unleaded 87 gasoline | NYMEX Chicago Unleaded Gasoline (Platts) vs. RBOB Gasoline futures contract (3C).<br>NYMEX Group Three Unleaded Gasoline (Platts) vs. RBOB Gasoline futures contract (A8). |
| | 2. Gulf Coast Conventional Blendstock for Oxygenated Blending (CBOB) 87. | NYMEX Gulf Coast CBOB Gasoline A1 (Platts) vs. RBOB Gasoline futures contract (CBA).<br>NYMEX Gulf Coast Unl 87 (Argus) Up-Down futures contract (UZ). |
| | 3. Gulf Coast CBOB 87 (Summer Assessment). | NYMEX Gulf Coast CBOB Gasoline A2 (Platts) vs. RBOB Gasoline futures contract (CRB). |
| | 4. Gulf Coast Unleaded 87 (Summer Assessment). | NYMEX Gulf Coast 87 Gasoline M2 (Platts) vs. RBOB Gasoline futures contract (RVG).<br>NYMEX Gulf Coast 87 Gasoline M2 (Platts) vs. RBOB Gasoline BALMO futures contract (GBB).<br>NYMEX Gulf Coast 87 Gasoline M2 (Argus) vs. RBOB Gasoline BALMO futures contract (RBG). |
| | 5. Gulf Coast Unleaded 87 | NYMEX Gulf Coast Unl 87 (Platts) Up-Down BALMO futures contract (1K).<br>NYMEX Gulf Coast Unl 87 Gasoline M1 (Platts) vs. RBOB Gasoline futures contract (RV).<br>CME Clearing Europe Gulf Coast Unleaded 87 Gasoline M1 (Platts) vs. New York RBOB Gasoline (NYMEX) Spread Calendar swap (ERV). |
| | 6. Los Angeles California Reformulated Blendstock for Oxygenate Blending (CARBOB) Regular. | NYMEX Los Angeles CARBOB Gasoline (OPIS) vs. RBOB Gasoline futures contract (JL). |
| | 7. Los Angeles California Reformulated Blendstock for Oxygenate Blending (CARBOB) Premium. | NYMEX Los Angeles CARBOB Gasoline (OPIS) vs. RBOB Gasoline futures contract (JL). |
| | 8. Euro-BOB OXY NWE Barges | NYMEX RBOB Gasoline vs. Euro-bob Oxy NWE Barges (Argus) (1000mt) futures contract (EXR).<br>CME Clearing Europe New York RBOB Gasoline (NYMEX) vs. European Gasoline Eurobob Oxy Barges NWE (Argus) (1000mt) Spread Calendar swap (EEXR). |
| | 9. Euro-BOB OXY FOB Rotterdam | ICE Futures Europe Gasoline Diff—RBOB Gasoline 1st Line vs. Argus Euro-BOB OXY FOB Rotterdam Barge Swap futures contract (ROE). |

## Appendix C to Part 150—Examples of Bona Fide Hedging Positions for Physical Commodities

A non-exhaustive list of examples meeting the definition of bona fide hedging position under § 150.1 is presented below. With respect to a position that does not fall within an example in this appendix, a person seeking to rely on a bona fide hedging position exemption under § 150.3 may seek guidance from the Division of Market Oversight. References to paragraphs in the examples below are to the definition of bona fide hedging position in § 150.1.

1. Portfolio Hedge Under Paragraph (3)(i) of the Bona Fide Hedging Definition

*Fact Pattern:* It is currently January and Participant A owns seven million bushels of corn located in its warehouses. Participant A has entered into fixed-price forward sale contracts with several processors for a total of five million bushels of corn that will be delivered by May of this year. Participant A has no fixed-price corn purchase contracts. Participant A's gross long cash position is equal to seven million bushels of corn. Because Participant A has sold forward five million bushels of corn, its net cash position is equal to long two million bushels of corn. To reduce price risk associated with potentially lower corn prices, Participant A chooses to establish a short position of 400 contracts in the CBOT Corn futures contract, equivalent to two million bushels of corn, in the same crop year as the inventory.

*Analysis:* The short position in a contract month in the current crop year for the CBOT Corn futures contract, equivalent to the amount of inventory held, satisfies the general requirements for a bona fide hedging position under paragraphs (2)(i)(A)–(C) and the provisions associated with owning a commodity under paragraph (3)(i).[1] Because the firm's net cash position is two million bushels of unsold corn, the firm is exposed to price risk. Participant A's hedge of the two million bushels represents a substitute for a fixed-price forward sale at a later time in the physical marketing channel. The position is economically appropriate to the reduction of price risk because the short position in a referenced contract does not exceed the quantity equivalent risk exposure (on a net basis) in the cash commodity in the current crop year. Last, the hedge arises from a potential change in the value of corn owned by Participant A.

2. Lending a Commodity and Hedge of Price Risk Under Paragraph (3)(i) of the Bona Fide Hedging Position Definition

*Fact Pattern:* Bank B owns 1,000 ounces of gold that it lends to Jewelry Fabricator J at LIBOR plus a differential. Under the terms of the loan, Jewelry Fabricator J may later purchase the gold from Bank B at a differential to the prevailing price of the Commodity Exchange, Inc. (COMEX) Gold futures contract (*i.e.,* an open-price purchase agreement is embedded in the terms of the loan). Jewelry Fabricator J intends to use the gold to make jewelry and reimburse Bank B for the loan using the proceeds from jewelry sales and either purchase gold from Bank B by paying the market price for gold or return the equivalent amount of gold to Bank B by purchasing gold at the market price. Because Bank B has retained the price risk on gold, the bank is concerned about its potential loss if the price of gold drops. The bank reduces the risk of a potential loss in the value of the gold by establishing a ten contract short position in the COMEX Gold futures contract, which has a unit of trading of 100 ounces of gold. The ten contract short position is equivalent to 1,000 ounces of gold.

*Analysis:* This position meets the general requirements for bona fide hedging positions under paragraphs (2)(i)(A)–(C) and the requirements associated with owning a cash commodity under paragraph (3)(i). The physical commodity that is being hedged is the underlying cash commodity for the COMEX Gold futures contract. Bank B's short hedge of the gold represents a substitute for a transaction to be made in the physical marketing channel (*e.g.,* completion of the open-price sale to Jewelry Fabricator J). Because the notional quantity of the short position in the gold futures contract is equal to the amount of gold that Bank B owns, the hedge is economically appropriate to the reduction of risk. Finally, the short position in the commodity derivative contract offsets the potential change in the value of the gold owned by Bank B.

3. Repurchase Agreements and Hedge of Inventory Under Paragraph (3)(i) of the Bona Fide Hedging Position Definition

*Fact Pattern:* Elevator A purchased 500,000 bushels of wheat in April and reduced its price risk by establishing a short position of 100 contracts in the CBOT Wheat futures contract, equivalent to 500,000 bushels of wheat. Because the price of wheat rose steadily since April, Elevator A had to make substantial maintenance margin payments. To alleviate its cash flow concern about meeting further margin calls, Elevator A decides to enter into a repurchase agreement with Bank B and offset its short position in the wheat futures contract. The repurchase agreement involves two separate contracts: a fixed-price sale from Elevator A to Bank B at today's spot price; and an open-price purchase agreement that will allow Elevator A to repurchase the wheat from Bank B at the prevailing spot price three months from now. Because Bank B obtains title to the wheat under the fixed-price purchase agreement, it is exposed to price risk should the price of wheat drop. Bank B establishes a short position of 100 contracts in the CBOT Wheat futures contract, equivalent to 500,000 bushels of wheat.

*Analysis:* Bank B's position meets the general requirements for a bona fide hedging position under paragraphs (2)(i)(A)–(C) and the provisions for owning the cash commodity under paragraph (3)(i). The short position in referenced contracts by Bank B is a substitute for a fixed-price sales transaction to be taken at a later time in the physical marketing channel either to Elevator A or to another commercial party. The position is economically appropriate to the reduction of risk in the conduct and management of the commercial enterprise (Bank B) because the notional quantity of the short position in referenced contracts held by Bank B is not larger than the quantity of cash wheat purchased by Bank B. Finally, the short position in the CBOT Wheat futures contract reduces the price risk associated with owning cash wheat.

4. Utility Hedge of Anticipated Customer Requirements Under Paragraph (3)(iii)(B) of the Bona Fide Hedging Position Definition

*Fact Pattern:* A Natural Gas Utility A, regulated by State Public Utility Commission, decides to hedge its purchases of natural gas in order to reduce natural gas price risk on behalf of its residential customers. State Public Utility Commission considers the hedging practice to be prudent and allows gains and losses from hedging to be passed on to Natural Gas Utility A's residential natural gas customers. Natural Gas Utility A has about one million residential customers who have average historical usage of about 71.5 mmBTUs of natural gas per year per residence. The utility decides to hedge about 70 percent of its residential customers' anticipated requirements for the following year, equivalent to a 5,000 contract long position in the NYMEX Henry Hub Natural Gas futures contract. To reduce the risk of higher prices to residential customers, Natural Gas Utility A establishes a 5,000 contract long position in the NYMEX Henry Hub Natural Gas futures contract. Since the utility is only hedging 70 percent of historical usage, Natural Gas Utility A is highly certain that realized demand will exceed its hedged anticipated residential customer requirements.

*Analysis:* Natural Gas Utility A's position meets the general requirements for a bona fide hedging position under paragraphs (2)(i)(A)–(C) and the provisions for hedges of unfilled anticipated requirements by a utility under paragraph (3)(iii)(B). The physical commodity that is being hedged involves a commodity underlying the NYMEX Henry Hub Natural Gas futures contract. The long position in the commodity derivative contract represents a substitute for transactions to be taken at a later time in the physical marketing channel. The position is economically appropriate to the reduction of price risk because the price of natural gas may increase. The commodity derivative contract position offsets the price risk of natural gas that the utility anticipates purchasing on behalf of its residential customers. As provided under paragraph (3)(iii), the risk-reducing position qualifies as a bona fide hedging position in the natural gas physical-delivery referenced contract during the spot month, provided that the position does not exceed the unfilled anticipated requirements for that month and for the next succeeding month.

[1] Participant A could also choose to hedge on a gross basis. In that event, Participant A could establish a short position in the March Chicago Board of Trade Corn futures contract equivalent to seven million bushels of corn to offset the price risk of its inventory and establish a long position in the May Chicago Board of Trade Corn futures contract equivalent to five million bushels of corn to offset the price risk of its fixed-price forward sale contracts.

5. Processor Margins Hedge Using Unfilled Anticipated Requirements Under Paragraph (3)(iii)(A) of the Bona Fide Hedging Position Definition and Anticipated Production Under Paragraph (4)(i) of the Definition

*Fact Pattern:* Soybean Processor A has a total throughput capacity of 200 million bushels of soybeans per year (equivalent to 40,000 CBOT soybean futures contracts). Soybean Processor A crushes soybeans into products (soybean oil and soybean meal). It currently has 40 million bushels of soybeans in storage and has offset that risk through fixed-price forward sales of the amount of products expected to be produced from crushing 40 million bushels of soybeans, thus locking in its processor margin on one million metric tons of soybeans. Because it has consistently operated its plants at full capacity over the last three years, it anticipates purchasing another 160 million bushels of soybeans to be delivered to its storage facility over the next year. It has not sold the 160 million bushels of anticipated production of crushed products forward. Processor A faces the risk that the difference in price relationships between soybeans and the crushed products (*i.e.,* the crush spread) could change adversely, resulting in reduced anticipated processing margins. To hedge its processing margins and lock in the crush spread, Processor A establishes a long position of 32,000 contracts in the CBOT Soybean futures contract (equivalent to 160 million bushels of soybeans) and corresponding short positions in CBOT Soybean Meal and Soybean Oil futures contracts, such that the total notional quantity of soybean meal and soybean meal futures contracts are equivalent to the expected production from crushing 160 million bushels of soybeans into soybean meal and soybean oil.

*Analysis:* These positions meet the general requirements for bona fide hedging positions under paragraphs (2)(i)(A)–(C) and the provisions for hedges of unfilled anticipated requirements under paragraph (3)(iii)(A) and unsold anticipated production under paragraph (4)(i). The physical commodities being hedged are commodities underlying the CBOT Soybean, Soybean Meal, and Soybean Oil futures contracts. Such positions are a substitute for purchases and sales to be made at a later time in the physical marketing channel and are economically appropriate to the reduction of risk. The positions in referenced contracts offset the potential change in the value of soybeans that the processor anticipates purchasing and the potential change in the value of products and by-products the processor anticipates producing and selling. The size of the permissible long hedge position in the soybean futures contract must be reduced by any inventories and fixed-price purchases because they would reduce the processor's *unfilled* requirements. Similarly, the size of the permissible short hedge positions in soybean meal and soybean oil futures contracts must be reduced by any fixed-price sales because they would reduce the processor's *unsold* anticipated production. As provided under paragraph (3)(iii)(A), the risk reducing long position in the soybean futures contract that is not in excess of the anticipated requirements for soybeans for that month and the next succeeding month qualifies as a bona fide hedging position during the last five days of trading in the physical-delivery referenced contract. As provided under paragraph (4)(i), the risk reducing short position in the soybean meal and oil futures contract do not qualify as a bona fide hedging position in a physical-delivery referenced contract during the last five days of trading in the event the Soybean Processor A does not have unsold products in inventory.

The combination of the long and short positions in soybean, soybean meal, and soybean oil futures contracts are economically appropriate to the reduction of risk. However, unlike in this example, an unpaired position (*e.g.,* only a long position in a commodity derivative contract) that is *not* offset by either a cash market position (*e.g.,* a fixed-price sales contract) or derivative position (*e.g.,* a short position in a commodity derivative contract) would not represent an economically appropriate reduction of risk. This is because the commercial enterprise's crush spread risk is relatively low in comparison to the price risk from taking an outright long position in the futures contract in the underlying commodity or an outright short position in the futures contracts in the products and by-products of processing. The price fluctuations of the crush spread, that is, the risk faced by the commercial enterprise, would not be expected to be substantially related to the price fluctuations of either an outright long or outright short futures position.

6. Agent Hedge Under Paragraph (3)(iv) of the Bona Fide Hedging Position Definition

*Fact Pattern:* Cotton Merchant A is in the business of merchandising (selling) cash cotton. Cotton Merchant A does not own any cash commodity, but has purchased the right to redeem a producer's cotton held as collateral by USDA (that is, ''cotton equities'') and, thereby, Cotton Merchant A has incurred price risk. A producer of cotton may borrow from the USDA's Commodity Credit Corporation, posting their cotton as collateral on the loan. USDA permits the producer to assign the right to redeem cotton held as collateral. Once Cotton Merchant A purchases from a producer the right to redeem cotton from USDA, Cotton Merchant A, in effect, is responsible for merchandising of the cash cotton held as collateral by USDA. For the volumes of cotton it is authorized to redeem from USDA, Cotton Merchant A enters into economically appropriate short positions in cotton commodity derivative contracts that offset the price risks of the cash commodities.

*Analysis:* The positions meet the requirements of paragraphs (2)(1)(A)–(C) for hedges of a physical commodity and paragraph (3)(iv) for hedges by an agent. The positions represent a substitute for transactions to be made in the physical marketing channel, are economically appropriate to the reduction of risks arising from cotton owned by the agent's contractual counterparties, and arise from the potential change in the value of such cotton. The agent does not own and has not contracted to purchase such cotton at a fixed price, but is responsible for merchandising the cash positions that are being offset in commodity derivative contracts. The agent has a contractual arrangement with the persons who own the cotton being offset.

7. Sovereign Hedge of a Pass-Through Swap Under Paragraph (2)(ii) of the Bona Fide Hedging Position Definition Opposite a Deemed Bona Fide Hedge of Unsold Anticipated Production Under Paragraph 4(i)

*Fact Pattern:* A Sovereign induces a farmer to sell his anticipated production of 100,000 bushels of corn forward to User A at a fixed price for delivery during the expected harvest, by, in effect, granting that farmer a cash-settled call option at no cost. In return for the farmer entering into the fixed-price forward sale at the prevailing market price, the Sovereign agrees to pay the farmer the difference between the market price at the time of harvest and the price of the fixed-price forward, in the event that the market price at the time of harvest is above the price of the forward. The fixed-price forward sale of 100,000 bushels of corn offsets the farmer's price risk associated with his anticipated agricultural production. The call option provides the farmer with upside price participation. The Sovereign faces commodity price risk from the option it granted at no cost to the farmer. To reduce that risk, the Sovereign establishes a long position of 20 call options on the Chicago Board of Trade (CBOT) Corn futures contract, equivalent to 100,000 bushels of corn.

*Analysis:* The farmer was induced by a long call option granted at no cost, in return for the farmer entering into a fixed-price forward sale at the prevailing market price.The risk profile of the combination of the forward sale and the long call is approximately equivalent to the risk profile of a synthetic long put.[2] A synthetic long put offsets the downside price risk of anticipated production. Under these circumstances of a Sovereign granting a call option to a farmer at no cost, the Commission deems the synthetic position of the farmer as satisfying the general requirements for a bona fide hedging position under paragraphs (2)(i)(A)–(C) and meeting the requirements for anticipated agricultural production under paragraph (4)(i), for purposes of the Sovereign's pass-through swap offset under paragraph (2)(ii). The agreement between the Sovereign and the farmer involves the production of a commodity underlying the CBOT Corn futures contract. Also under these circumstances, the Commission deems the synthetic long put as a substitute for transactions that the farmer has made in the physical marketing channel, because a long put would reduce the price risk associated with the farmer's anticipated agricultural production.

The Sovereign is the counterparty to the farmer, who under these circumstances the Commission deems to be a bona fide hedger for purposes of the Sovereign's pass-through swap offset. That is, the Commission considers the Sovereign's long call position to be a pass-through swap meeting the

[2] Put-call parity describes the mathematical relationship between price of a put and call with identical strike prices and expiry.

requirements of paragraph (2)(ii)(B). As provided under paragraph (2)(ii)(A), the Sovereign's risk-reducing position in the CBOT Corn option would qualify as a pass-through swap offset as a bona fide hedging position, or, alternatively, if the pass-through swap is not a referenced contract, then the pass-through swap offset may qualify as a cross-commodity hedge under paragraph (5), provided the fluctuations in value of the pass-through swap offset are substantially related to the fluctuations in value of the pass-through swap. Such a pass-through swap offset will not qualify as a bona fide hedging position in a physical-delivery futures contract during the last five days of trading under paragraphs (2)(iii)(B) or (5); however, since the CBOT Corn option will exercise into a physical-delivery CBOT Corn futures contract prior to the last five days of trading in that physical-delivery futures contract, the Sovereign may continue to hold its option position as a bona fide hedging position through option expiry.

8. Hedge of Offsetting Unfixed Price Sales and Purchases Under Paragraph (4)(ii) of the Bona Fide Hedging Position Definition

*Fact Pattern:* Currently it is October and Oil Merchandiser A has entered into cash forward contracts to purchase 600,000 of crude oil at a floating price that references the January contract month (in the next calendar year) for the ICE Futures Brent Crude futures contract and to sell 600,000 barrels of crude oil at a price that references the February contract month (in the next calendar year) for the NYMEX Light Sweet Crude Oil futures contract. Oil Merchandiser A is concerned about an adverse change in the price spread between the January ICE Futures Brent Crude futures contract and the February NYMEX Light Sweet Crude Oil futures contract. To reduce that risk, Oil Merchandiser A establishes a long position of 600 contracts in the January ICE Futures Brent Crude futures contract, price risk equivalent to buying 600,000 barrels of oil, and a short position of 600 contracts in the February NYMEX Light Sweet Crude Oil futures contract, price risk equivalent to selling 600,000 barrels of oil.

*Analysis:* Oil Merchandiser A's positions meet the general requirements for bona fide hedging positions under paragraphs (2)(i)(A)–(C) and the provisions for offsetting sales and purchases in referenced contracts under paragraph (4)(ii). The physical commodity that is being hedged involves a commodity underlying the NYMEX Light Sweet Crude Oil futures contract. The long and short positions in commodity derivative contracts represent substitutes for transactions to be taken at a later time in the physical marketing channel. The positions are economically appropriate to the reduction of risk because the price spread between the ICE Futures Brent Crude futures contract and the NYMEX Light Sweet Crude Oil futures contract could move adversely to Oil Merchandiser A's interests in the two cash forward contracts, that is, the price of the ICE Futures Brent Crude futures contract could increase relative to the price of the NYMEX Light Sweet Crude Oil futures contract. The positions in commodity derivative contracts offset the price risk in the cash forward contracts. As provided under paragraph (4), the risk-reducing position does not qualify as a bona fide hedging position in the crude oil physical-delivery referenced contract during the spot month.

9. Anticipated Royalties Hedge Under Paragraph (4)(iii) of the Bona Fide Hedging Position Definition and Pass-Through Swaps Hedge Under Paragraph (2)(ii) of the Definition

a. *Fact Pattern:* In order to develop an oil field, Company A approaches Bank B for financing. To facilitate the loan, Bank B first establishes an independent legal entity commonly known as a special purpose vehicle (SPV). Bank B then provides a loan to the SPV. The SPV is obligated to repay principal and interest to the Bank based on a fixed price for crude oil. The SPV in turn makes a production loan to Company A. The terms of the production loan require Company A to provide the SPV with volumetric production payments (VPPs) based on a specified share of the production to be sold at the prevailing price of crude oil (*i.e.,* the index price) as oil is produced. Because the price of crude oil may fall, the SPV reduces that risk by entering into a crude oil swap with Swap Dealer C. The swap requires the SPV to pay Swap Dealer C the floating price of crude oil (*i.e.,* the index price) and for Swap Dealer C to pay a fixed price to the SPV. The notional quantity for the swap is equal to the expected production underlying the VPPs to the SPV. The SPV will receive a floating price at index on the VPP and will pay a floating price at index on the swap, which will offset. The SPV will receive a fixed price payment on the swap and repay the loan's principal and interest to Bank B. The SPV is highly certain that the VPP production volume will occur, since the SPV's engineer has reviewed the forecasted production from Company A and required the VPP volume to be set with a cushion (*i.e.,* a hair-cut) below the forecasted production.

*Analysis:* For the SPV, the swap between Swap Dealer C and the SPV meets the general requirements for a bona fide hedging position under paragraphs (2)(i)(A)–(C) and the requirements for anticipated royalties under paragraph (4)(iii). The SPV will receive payments under the VPP royalty contract based on the unfixed price sale of anticipated production of the physical commodity underlying the royalty contract, *i.e.,* crude oil. The swap represents a substitute for the price of sales transactions to be made in the physical marketing channel. The SPV's swap position qualifies as a hedge because it is economically appropriate to the reduction of price risk. The swap reduces the price risk associated with a change in value of a royalty asset. The fluctuations in value of the SPV's anticipated royalties are substantially related to the fluctuations in value of the crude oil swap with Swap Dealer C.

b. *Continuation of Fact Pattern:* Swap Dealer C offsets the price risk associated with the swap to the SPV by establishing a short position in cash-settled crude oil futures contracts. The notional quantity of the short position in futures contracts held by Swap Dealer C exactly matches the notional quantity of the swap with the SPV.

*Analysis:* For the swap dealer, because the SPV enters the cash-settled swap as a bona fide hedger under paragraph (4)(iii) (*i.e.,* a pass-through swap counterparty), the offset of the risk of the swap in a futures contract by Swap Dealer C qualifies as a bona fide hedging position (*i.e.,* a pass-through swap offset) under paragraph (2)(ii)(A). Since the swap was executed opposite a pass-through swap counterparty and was offset, the swap itself also qualifies as a bona fide hedging position (*i.e.,* a pass-through swap) under paragraph (2)(ii)(B). If the cash-settled swap is not a referenced contract, then the pass-through swap offset may qualify as a cross-commodity hedge under paragraph (5), provided the fluctuations in value of the pass-through swap offset are substantially related to the fluctuations in value of the pass-through swap.

10. Anticipated Royalties Hedge Under Paragraph (4)(iii) of the Bona Fide Hedging Position Definition and Cross-Commodity Hedge Under Paragraph (5) of the Definition

*Fact Pattern:* An eligible contract participant (ECP) owns royalty interests in a portfolio of oil wells. Royalties are paid at the prevailing (floating) market price for the commodities produced and sold at major trading hubs, less transportation and gathering charges. The large portfolio and well-established production history for most of the oil wells provide a highly certain production stream for the next 24 months. The ECP also determined that changes in the cash market prices of 50 percent of the oil production underlying the portfolio of royalty interests historically have been closely correlated with changes in the calendar month average of daily settlement prices of the nearby NYMEX Light Sweet Crude Oil futures contract. The ECP decided to hedge some of the royalty price risk by entering into a cash-settled swap with a term of 24 months. Under terms of the swap, the ECP will receive a fixed payment and make monthly payments based on the calendar month average of daily settlement prices of the nearby NYMEX Light Sweet Crude Oil futures contract and notional amounts equal to 50 percent of the expected production volume of oil underlying the royalties.

*Analysis:* This position meets the requirements of paragraphs (2)(i)(A)–(C) for hedges of a physical commodity, paragraph (4)(iii) for hedges of anticipated royalties, and paragraph (5) for cross-commodity hedges. The long position in the commodity derivative contract represents a substitute for transactions to be taken at a later time in the physical marketing channel. The position is economically appropriate to the reduction of price risk because the price of oil may decrease. The commodity derivative contract position offsets the price risk of royalty payments, based on oil production, that the ECP anticipates receiving. The ECP is exposed to price risk arising from the anticipated production volume of oil attributable to her royalty interests. The physical commodity underlying the royalty portfolio that is being hedged involves a commodity with fluctuations in value that are substantially related to the fluctuations in value of the swap.

11. Hedges of Services Under Paragraph (4)(iv) of the Bona Fide Hedging Position Definition

a. *Fact Pattern:* Company A enters into a risk service agreement to drill an oil well with Company B. The risk service agreement provides that a portion of the revenue receipts to Company A depends on the value of the light sweet crude oil produced. Company A is exposed to the risk that the price of oil may fall, resulting in lower anticipated revenues from the risk service agreement. To reduce that risk, Company A establishes a short position in the New York Mercantile Exchange (NYMEX) Light Sweet Crude Oil futures contract, in a notional amount equivalent to the firm's anticipated share of the expected quantity of oil to be produced. Company A is highly certain of its anticipated share of the expected quantity of oil to be produced.

*Analysis:* Company A's hedge of a portion of its revenue stream from the risk service agreement meets the general requirements for bona fide hedging positions under paragraphs (2)(i)(A)–(C) and the provisions for services under paragraph (4)(iv). The contract for services involves the production of a commodity underlying the NYMEX Light Sweet Crude Oil futures contract. A short position in the NYMEX Light Sweet Crude Oil futures contract is a substitute for transactions to be taken at a later time in the physical marketing channel, with the value of the revenue receipts to Company A dependent on the price of the oil sales in the physical marketing channel. The short position in the futures contract held by Company A is economically appropriate to the reduction of risk, because the total notional quantity underlying the short position in the futures contract held by Company A is equivalent to its share of the expected quantity of future production under the risk service agreement. Because the price of oil may fall, the short position in the futures contract reduces price risk from a potential reduction in the payments to Company A under the service contract with Company B. Under paragraph (4)(iv), the risk-reducing position will not qualify as a bona fide hedging position during the spot month of the physical-delivery oil futures contract.

b. *Fact Pattern:* A City contracts with Firm A to provide waste management services. The contract requires that the trucks used to transport the solid waste use natural gas as a power source. According to the contract, the City will pay for the cost of the natural gas used to transport the solid waste by Firm A. In the event that natural gas prices rise, the City's waste transport expenses will increase. To mitigate this risk, the City establishes a long position in the NYMEX Henry Hub Natural Gas futures contract in an amount equivalent to the expected volume of natural gas to be used over the life of the service contract.

*Analysis:* This position meets the general requirements for bona fide hedging positions under paragraphs (2)(i)(A)–(C) and the provisions for services under paragraph (4)(iv). The contract for services involves the use of a commodity underlying the NYMEX Henry Hub Natural Gas futures contract. Because the City is responsible for paying the cash price for the natural gas used under the services contract, the long hedge is a substitute for transactions to be taken at a later time in the physical marketing channel. The position is economically appropriate to the reduction of price risk because the total notional quantity of the long position in a commodity derivative contract equals the expected volume of natural gas to be used over the life of the contract. The position in the commodity derivative contract reduces the price risk associated with an increase in anticipated costs that the City may incur under the services contract in the event that the price of natural gas increases. As provided under paragraph (4), the risk reducing position will not qualify as a bona fide hedge during the spot month of the physical-delivery futures contract.

12. Cross-Commodity Hedge Under Paragraph (5) of the Bona Fide Hedging Position Definition and Inventory Hedge Under Paragraph (3)(i) of the Definition

*Fact Pattern:* Copper Wire Fabricator A is concerned about possible reductions in the price of copper. Currently it is November and it owns inventory of 100 million pounds of copper and 50 million pounds of finished copper wire. Copper Wire Fabricator A expects to sell 150 million pounds of finished copper wire in February of the following year. To reduce its price risk, Copper Wire Fabricator A establishes a short position of 6,000 contracts in the February COMEX Copper futures contract, equivalent to selling 150 million pounds of copper. The fluctuations in value of copper wire are expected to be substantially related to fluctuations in value of copper.

*Analysis:* The Copper Wire Fabricator A's position meets the general requirements for a bona fide hedging position under paragraphs (2)(i)(A)–(C) and the provisions for owning a commodity under paragraph (3)(i) and for a cross-hedge of the finished copper wire under paragraph (5). The short position in a referenced contract represents a substitute for transactions to be taken at a later time in the physical marketing channel. The short position is economically appropriate to the reduction of price risk in the conduct and management of the commercial enterprise because the price of copper could drop. The short position in the referenced contract offsets the risk of a possible reduction in the value of the inventory that it owns. Since the finished copper wire is a product of copper that is not deliverable on the commodity derivative contract, 2,000 contracts of the short position are a cross-commodity hedge of the finished copper wire and 4,000 contracts of the short position are a hedge of the copper inventory.

13. Cross-Commodity Hedge Under Paragraph (5) of the Bona Fide Hedging Position Definition and Anticipated Requirements Hedge Under Paragraph (3)(iii)(A) of the Definition

*Fact Pattern:* Airline A anticipates using a predictable volume of jet fuel every month based on scheduled flights and decides to hedge 80 percent of that volume for each of the next 12 months. After a review of various commodity derivative contract hedging strategies, Airline A decides to cross hedge its anticipated jet fuel requirements in ultra-low sulfur diesel (ULSD) commodity derivative contracts. Airline A determined that price fluctuations in its average cost for jet fuel were substantially related to the price fluctuations of the calendar month average of the first nearby physical-delivery NYMEX New York Harbor ULSD Heating Oil (HO) futures contract and determined an appropriate hedge ratio, based on a regression analysis, of the HO futures contract to the quantity equivalent amount of its anticipated requirements. Airline A decided that it would use the HO futures contract to cross hedge part of its jet fuel price risk. In addition, Airline A decided to protect against jet fuel price increases by cross hedging another part of its anticipated jet fuel requirements with a long position in cash-settled calls in the NYMEX Heating Oil Average Price Option (AT) contract. The AT call option is settled based on the price of the HO futures contract. The sum of the notional amounts of the long position in AT call options and the long position in the HO futures contract will not exceed the quantity equivalent of 80 percent of Airline A's anticipated requirements for jet fuel.

*Analysis:* The positions meet the requirements of paragraphs (2)(i)(A)–(C) for hedges of a physical commodity, paragraph (3)(iii)(A) for unfilled anticipated requirements and paragraph (5) for cross-commodity hedges. The positions represent a substitute for transactions to be made in the physical marketing channel, are economically appropriate to the reduction of risks arising from anticipated requirements for jet fuel, and arise from the potential change in the value of such jet fuel. The aggregation notional amount of the airline's positions in the call option and the futures contract does not exceed the quantity equivalent of anticipated requirements for jet fuel. The value fluctuations in jet fuel are substantially related to the value fluctuations in the HO futures contract.

Airline A may hold its long position in the cash-settled AT call option contract as a cross hedge against jet fuel price risk without having to exit the contract during the spot month.

14. Position Aggregation Under § 150.4 and Inventory Hedge Under Paragraph (3)(i) of the Bona Fide Hedging Position Definition

*Fact Pattern:* Company A owns 100 percent of Company B. Company B buys and sells a variety of agricultural products, including wheat. Company B currently owns five million bushels of wheat. To reduce some of its price risk, Company B establishes a short position of 600 contracts in the CBOT Wheat futures contract, equivalent to three million bushels of wheat. After communicating with Company B, Company A establishes an additional short position of 400 CBOT Wheat futures contracts, equivalent to two million bushels of wheat.

*Analysis:* The aggregate short position in the wheat referenced contract held by Company A and Company B meets the general requirements for a bona fide hedging position under paragraphs (2)(i)(A)–(C) and the provisions for owning a cash commodity under paragraph (3)(i). Because Company A owns more than 10 percent of Company B, Company A and B are aggregated together as one person under § 150.4. Entities required to aggregate accounts or positions under § 150.4 are the same person for the purpose of determining whether a person is eligible for a bona fide hedging position exemption under § 150.3. The aggregate short position in the futures contract held by Company A and Company B represents a substitute for transactions to be taken at a later time in the physical marketing channel. The aggregate short position in the futures contract held by Company A and Company B is economically appropriate to the reduction of price risk because the aggregate short position in the CBOT Wheat futures contract held by Company A and Company B, equivalent to five million bushels of wheat, does not exceed the five million bushels of wheat that is owned by Company B. The price risk exposure for Company A and Company B results from a potential change in the value of that wheat.

## Appendix D to Part 150—Initial Position Limit Levels

| Contract | Spot-month | Single month and all months |
|---|---|---|
| Legacy Agricultural: | | |
| Chicago Board of Trade Corn (C) | 600 | 62,400 |
| Chicago Board of Trade Oats (O) | 600 | 5,000 |
| Chicago Board of Trade Soybeans (S) | 600 | 31,900 |
| Chicago Board of Trade Soybean Meal (SM) | 720 | 16,900 |
| Chicago Board of Trade Soybean Oil (SO) | 540 | 16,700 |
| Chicago Board of Trade Wheat (W) | 600 | 32,800 |
| ICE Futures U.S. Cotton No. 2 (CT) | 1,600 | 9,400 |
| Chicago Board of Trade KC HRW Wheat (KW) | 600 | 12,000 |
| Minneapolis Grain Exchange Hard Red Spring Wheat (MWE) | 1,000 | 12,000 |
| Other Agricultural: | | |
| Chicago Board of Trade Rough Rice (RR) | 600 | 5,000 |
| Chicago Mercantile Exchange Live Cattle (LC) | 450 | 12,200 |
| ICE Futures U.S. Cocoa (CC) | 5,500 | 10,200 |
| ICE Futures U.S. Coffee C (KC) | 2,400 | 8,800 |
| ICE Futures U.S. FCOJ–A (OJ) | 2,800 | 5,000 |
| ICE Futures U.S. Sugar No. 11 (SB) | 23,300 | 38,400 |
| ICE Futures U.S. Sugar No. 16 (SF) | 7,000 | 7,000 |
| Energy: | | |
| New York Mercantile Exchange Henry Hub Natural Gas (NG) | 2,000 | 200,900 |
| New York Mercantile Exchange Light Sweet Crude Oil (CL) | 10,400 | 148,800 |
| New York Mercantile Exchange NY Harbor ULSD (HO) | 2,900 | 21,300 |
| New York Mercantile Exchange RBOB Gasoline (RB) | 6,800 | 15,300 |
| Metal: | | |
| Commodity Exchange, Inc. Copper (HG) | 1,000 | 7,800 |
| Commodity Exchange, Inc. Gold (GC) | 6,000 | 19,500 |
| Commodity Exchange, Inc. Silver (SI) | 3,000 | 7,600 |
| New York Mercantile Exchange Palladium (PA) | 100 | 5,000 |
| New York Mercantile Exchange Platinum (PL) | 500 | 5,000 |

## Appendix E To Part 150—Guidance Regarding Exchange-Set Speculative Position Limits

Guidance for Designated Contract Markets

(1) Until such time that a boards of trade has access to sufficient swap position information, a board of trade need not demonstrate compliance with Core Principle 5 with respect to swaps. A board of trade should have access to sufficient swap position information if, for example: (1) It had access to daily information about its market participants' open swap positions; or (2) it knows that its market participants regularly engage in large volumes of speculative trading activity, including through knowledge gained in surveillance of heavy trading activity, that would cause reasonable surveillance personnel at an exchange to inquire further about a market participant's intentions or total open swap positions.

(2) When a board of trade has access to sufficient swap position information, this guidance would no longer be applicable. At such time, a board of trade is required to file rules with the Commission to implement the relevant position limits and demonstrate compliance with Core Principle 5(A) and (B).

Guidance for Swap Execution Facilities

(1) Until such time that a swap execution facility that is a trading facility has access to sufficient swap position information, the swap execution facility need not demonstrate compliance with Core Principle 6(A) or (B). A swap execution facility should have access to sufficient swap position information if, for example: (1) It had access to daily information about its market participants' open swap positions; or (2) if it knows that its market participants regularly engage in large volumes of speculative trading activity, including through knowledge gained in surveillance of heavy trading activity, that would cause reasonable surveillance personnel at an exchange to inquire further about a market participant's intentions or total open swap positions.

(2) When a swap execution facility has access to sufficient swap position information, this guidance would no longer be applicable. At such time, a swap execution facility is required to file rules with the Commission to implement the relevant position limits and demonstrate compliance with Core Principle 6(A) and (B).

## PART 151—[REMOVED AND RESERVED]

■ 29. Under the authority of section 8a(5) of the Commodity Exchange Act, 7 U.S.C. 12a(5), remove and reserve part 151.

Issued in Washington, DC, on December 5, 2016, by the Commission.

**Christopher J. Kirkpatrick,**

*Secretary of the Commission.*

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

## Appendices to Position Limits for Derivatives—Commission Voting Summary, Chairman's Statement, and Commissioners' Statements

## Appendix 1—Commission Voting Summary

On this matter, Chairman Massad and Commissioners Bowen and Giancarlo voted in the affirmative. No Commissioner voted in the negative.

## Appendix 2—Statement of Chairman Timothy G. Massad

Today, the Commission is issuing a revised position limits proposal. We are also finalizing a separate but related rule on the aggregation of positions. I am pleased that today's actions are unanimous.

Congress directed us to implement a position limits rule to limit excessive speculation. While speculators play a necessary and important role in our markets, position limits can prevent the type of excessive speculation by a few large participants that leads to corners, squeezes and other activity that can distort markets and be unfair to other participants. Position limits can also promote convergence without compromising market liquidity. There are many issues to consider in this rule, but position limits are not a new or untested concept. They have been in place in our markets for decades, either through federal limits or exchange-set limits, and they have worked well.

There are two reasons why I am supporting issuing a reproposal. First, we have made many changes to the 2013 proposal we inherited that are reflected in today's reproposal. Certain aspects have been previously proposed in separate pieces, and I believe the public would benefit from seeing the proposal in its entirety, to better understand how the various changes work together.

Second, the Commission is now in a time of transition. I do not want to adopt a final rule today that the Commission would choose not to implement or defend next year. Our markets and the many end-users and consumers who rely on them are served best by having reasonable and predictable regulation. Uncertainty and inconsistency from one year to the next are not helpful.

Our staff has done a tremendous amount of work to devise a position limits rule that meets the requirements of the law and balances the various concerns at stake. This work has spanned several years, involved review of literally thousands of pages of comments from participants, and included many meetings and public roundtables.

Commissioners Bowen, Giancarlo, and I have also spent substantial time on this issue. We took office together in June 2014 and inherited a proposal that the Commission had issued six months before. As I promised then, we have been working hard to get the rule right. In addition to discussing the issues extensively with staff, we have each had many meetings with market participants and other members of the public. We have each traveled around the country and heard from users of these markets. In particular, I have heard from many smaller, traditional users about the importance of position limits. I have also had the benefit of sponsoring the Agricultural Advisory Committee, whose members have provided important input on these issues.

We have revised the proposed limits themselves in light of substantial work our staff has done to make sure they are based on the latest and best information as to estimated deliverable supply. We have considered a wide range of information, including the recommendations of the exchanges and other data to which the exchanges do not have access. For some contracts, the proposed limits for the spot month are higher than the exchange-set limits today. There have been, for example, substantial increases in estimates of deliverable supply in the energy sector. In other cases, we have accepted recommendations of the exchanges to set federal limits that are actually lower than 25 percent of deliverable supply, because we determined that the requested lower limit was consistent with the overall policy goals and would not compromise market liquidity.

We have proposed further adjustments to the bona fide hedging position definition, to eliminate certain requirements that we have decided are unnecessary, and to address other concerns raised by market participants.

Another substantial difference from the 2013 text is our proposal first made this summer to allow the exchanges to grant non-enumerated hedge exemptions. This process must be subject to our oversight as a matter of law and as a matter of policy, given the inherent tension in the roles of the exchanges as market overseers and beneficiaries of higher trading volumes.

The proposal we are issuing today provides extensive analysis of the impact of the proposed spot and all months limits, which I believe supports the view that the limits should not compromise liquidity while addressing excessive speculation. The analysis shows few existing positions would exceed the limits, and that is without considering possible exemptions.

I recognize there will still be those that are critical of the proposal. Some will complain simply because of the length of the proposal—even though most of that is not rule text, but rather the summaries of the extensive comments and analysis required by law. Others may suggest broadening the bona fide hedge exemption so that it encompasses practically any activity with a business purpose, which is not what Congress said in the law. Still others will argue position limits are not necessary. But while the Commission should consider all comments, it is important to remember that the Commission has a responsibility to implement a balanced rule that achieves the objectives Congress has established.

Finally, while the Commission works to finalize this rule, we still have federal limits for nine agricultural commodities and exchange-set spot month limits for all the physical delivery contracts covered by this rule, which the Commission will continue to enforce.

I want to thank the staff again for their extensive work on this rule, particularly our staff in the Division of Market Oversight, the Office of the Chief Economist and the Office of the General Counsel. Their expertise and dedication on this matter is truly exemplary. I also want to thank Commissioners Bowen and Giancarlo for their very constructive engagement on this issue.

## Appendix 3—Statement of Commissioner Sharon Y. Bowen

With today's repreposal, the Commission moves one step closer to the implementation of position limits as directed by Congress in 2010. CFTC staff has worked laboriously with market users and the exchanges we regulate to craft a rule that will protect investors from disruptive practices and manipulation, while simultaneously allowing our markets to serve their critical price-discovery function. I commend staff on their hard work and thank the hundreds of commenters for their insightful feedback. I would also like to thank Chairman Massad and Commissioner Giancarlo on their commitment to this important rule and look forward to its finalization in the near future.

## Appendix 4—Statement of Commissioner J. Christopher Giancarlo

Since taking my seat on the Commission, I have traveled to well over a dozen states where I met with many family farmers and toured numerous energy utilities and manufacturing facilities. I have heard the concerns of agriculture and energy producers and consumers about market speculation and the role of position limits.

I have always been open to supporting a well-conceived and practical position limits rule that restricts excessive speculation. That is so long as it protects the ability of America's farmers, ranchers and processors to hedge risks of agricultural commodities and the ability of America's energy producers and distributors to control risks of energy production, storage and distribution.

That is why I believe it is so important to carefully consider the impact of this very complex rule on America's almost nine thousand grain elevators,[1] two million family farms[2] and 147 million electric utility customers.[3] That is why I support putting out this rule as a proposal.

My concern regarding previous earlier proposals has been that they would restrict bona fide hedging activity or harm America's agriculture and energy industries that have been sorely impacted by plummeting commodity prices and service provider consolidation. I am simply not willing to support a poorly designed and unworkable rule that ever after needs to be adjusted through a series of no-action letters and ad hoc staff interpretations and advisories that had become too common at the CFTC in prior years.

While some may view position limits as the ''eternal rule,'' I disagree. The current proposal is very detailed and highly complex. It is over 700 pages in length and has over one thousand footnotes. In some areas, concerns expressed by market participants regarding the 2011 rule that was struck down by the court and the 2013 proposal have been well addressed. In other

[1] U.S. Grain Storage Data, National Grain and Feed Association Web site (last visited Dec. 5, 2016), *https://www.ngfa.org/news-policy-center/resources/grain-industry-data/*.

[2] News Release, Family Farms are the Focus of New Agriculture Census Data, U.S. Department of Agriculture, Mar. 17, 2015, *http://www.usda.gov/wps/portal/usda/usdamediafb?contentid=2015/03/0066.xml&printable=true*.

[3] 2015–2016 Annual Directory & Statistical Report, American Public Power Association, at 26 (2016), *http://www.publicpower.org/files/PDFs/USElectricUtilityIndustryStatistics.pdf*.

areas, they do not appear to have been as well addressed.

Notably, the proposal introduces a series of new estimates of deliverable supply that have not been previously presented to the public. It also incorporates concepts introduced in the 2016 supplemental proposal. Given these new additions and the complexity of the proposal, one more round of public comment is appropriate.

I feel comfortable that the proposal before us provides the basis for the implementation of a final position limits rule that I could support. I commend the staff responsible for this proposal for all their hard work in making the significant improvements that are before us. I also extend my gratitude to Chairman Massad and Commissioner Bowen for agreeing to put this proposal before the public for comment.

I welcome commenters' views on the proposal. I expect that with their added insight we can finalize a position limits rule in 2017 that is workable and does not undo years of standard practice in these markets.

[FR Doc. 2016–29483 Filed 12–29–16; 8:45 am]

**BILLING CODE 6351–01–P**