Futures Industry Association
2001 Pennsylvania Ave. NW
Suite 600
Washington, DC 20006-1823

202.466.5460
202.296.3184 fax
www.futuresindustry.org

February 6, 2014

Via Electronic Submission

Melissa Jurgens, Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Aggregation of Positions (RIN 3038-AD82)

Dear Ms. Jurgens:

The Futures Industry Association, Inc. ("FIA") appreciates the opportunity to provide the Commodity Futures Trading Commission ("CFTC" or "Commission") with the comments and recommendations set forth below in response to the Commission's Notice of Proposed Rulemaking concerning Aggregation of Positions ("Aggregation Proposal").[1] By separate letter, FIA also is commenting on the Commission's related rulemaking regarding Position Limits on Derivatives ("2013 Position Limits Proposal").[2] Due to the interrelated nature of several aspects of the Aggregation and 2013 Position Limits Proposals, FIA requests that the Commission consider and address FIA's comments on both proposals together when finalizing these two rulemakings.

FIA appreciates the Commission's willingness to modify its 2012 Proposed Aggregation Rule in response to comments from market participants concerning the former Part 151 aggregation rules. The opportunity for constructive public comment will provide the Commission with the best opportunity to develop commercially practical rules that meet its policy objectives with lower costs and fewer unintended consequences for market participants. FIA's comments and recommendations focus on the practical impact that the Aggregation Proposal would have on participants in the listed and over-the-counter ("OTC") derivatives markets.

---

[1] *Aggregation of Positions*, 78 Fed. Reg. 68946 (Nov. 15, 2013).

[2] *Position Limits for Derivatives*, 78 Fed. Reg. 75680 (Dec. 12, 2013).

I. Interest of FIA in the Commission's Proposed Position Limits

FIA's regular and associate members, their affiliates, and their customers actively participate in the listed and OTC derivatives markets as intermediaries, principals, and users.[3] Consequently, FIA and its members have a significant interest in any position limits rules that the Commission proposes, including the Aggregation Proposal. As the Commission is aware, FIA provided the Commission with detailed comments concerning the Commission's January 2011 position limits proposal,[4] the November 2011 interim final position limits rules,[5] and the May 2012 proposed amendments to its position limits aggregation requirements.[6] FIA also supported the petitions filed by market participants requesting relief under section 4a(a)(7) of the Commodity Exchange Act, as amended ("CEA"), for certain commonly used hedging transactions.[7] FIA hereby incorporates by reference the comments listed above in this comment letter.

II. Summary of FIA's Comments

FIA generally supports the Aggregation Proposal because it incorporates or addresses many of the comments and recommendations made by FIA and other market participants concerning the Commission's prior proposed amendments to its aggregation rules. In particular, and subject to the recommendations and qualifications discussed in greater detail below, FIA supports:

---

[3] FIA is the leading trade organization for the futures, options and OTC cleared derivatives markets. FIA members are active users of the commodity futures markets and include derivatives clearing firms of all sizes as well as leading derivatives exchanges and large commodity firms. Given the variety of enterprises that comprise our regular and associate members, FIA is the only association representative of all organizations that have an interest in the cleared derivatives markets.

[4] *See Position Limits for Derivatives*, 76 Fed. Reg. 4752 (Jan. 26, 2011) (proposed rule); *see also* Letter from FIA, to Commodity Futures Trading Comm'n (Mar. 25, 2011), *available at* http://www.futuresindustry.org/downloads/FIA_Position_Limits_Comment_Letter.pdf; Letter from FIA, to Commodity Futures Trading Comm'n (May 25, 2011), *available at* http://www.futuresindustry.org/downloads/AggregationPositionLimitsforDerivatives052511.pdf.

[5] *See Position Limits for Futures and Swaps*, 76 Fed. Reg. 71626 (Nov. 18, 2011) ("2011 Position Limits Rule"); *see also* Letter from FIA, to Commodity Futures Trading Comm'n (Jan. 17, 2012), *available at* http://www.futuresindustry.org/downloads/FIA_InteriPositionLimitsonCash-SettledContracts.pdf.

[6] *See Aggregation, Position Limits for Futures and Swaps*, 77 Fed. Reg. 31767 (May 30, 2012) ("2012 Proposed Aggregation Rule"); *see also* Letter from FIA, to Commodity Futures Trading Comm'n (June 29, 2012), *available at* http://www.futuresindustry.org/downloads/Aggregation-NOPR-Comments-062912.pdf.

[7] *See* Petition from Working Group of Commercial Energy Firms, to Commodity Futures Trading Comm'n (Jan. 20, 2012), *available at* http://www.cftc.gov/stellent/groups/public/@rulesandproducts/documents/ifdocs/wgbfhpetition012012.pdf; *see also* Petition from FIA, to Commodity Futures Trading Comm'n (Mar. 26, 2012), *available at* http://www.futuresindustry.org/downloads/WorkingGroupPetitions032612.pdf.

- The exemption from aggregation for certain minority-owned entities. FIA supports the exemption from the aggregation requirement for independently controlled owned entities where the ownership or equity interest is not greater than 50 percent. In addition, FIA generally supports the interpretive guidance provided by the Commission in the preamble to the proposed rule that clarifies, in practical terms, the circumstances under which the CFTC will consider an owned entity to have: (1) "separately developed and independent trading systems;" (2) no shared employees; (3) "separate physical locations;" and (4) risk management systems that do not permit the sharing of trades or trading strategies.

- The new exemption from aggregation for certain majority-owned entities. FIA supports, with the caveats discussed below, an exemption from the aggregation requirement for majority-owned entities that are able to demonstrate independent management and control.

- The exemption from aggregation for information-sharing restrictions. FIA supports the exemption from the aggregation requirement for information-sharing restrictions, including the provision that permits market participants to prepare a memorandum of law, rather than a formal opinion of counsel, describing the basis for their conclusion that the sharing of information could create a reasonable risk of violating federal, state, or foreign laws or regulations adopted thereunder. FIA also supports the proposal to permit the memorandum of law to be prepared by either internal or external counsel, and "in a general manner" by a group of similarly situated market participants, rather than individually by every market participant for which the exemption would be available.[8]

- Exclusion of contingent ownership interests from the aggregation requirement. FIA supports the Commission's clarification that a contingent ownership interest, such as a call option for an equity stake in another market participant, does not constitute an ownership or equity interest for purposes of the Aggregation Proposal.

FIA respectfully submits that the Commission should improve the Aggregation Proposal by adopting the following clarifications and amendments in the final rule:

- Acting pursuant to an expressed or implied agreement. FIA requests that the Commission affirm, consistent with prior precedent, that the aggregation requirement applicable to "positions held by, and trading done by, two or more persons acting pursuant to an express or implied agreement or understanding" only applies when the parties agree to trade Referenced Contracts pursuant to such an agreement or

---

8 *See* Aggregation Proposal at 68950 ("Under the proposed rule, such a memorandum . . . could be provided by various persons to satisfy the requirement, so long as it is clear from the memorandum how the risk applies to the person providing the memorandum.").

understanding. In particular, FIA requests that the Commission revise the discussion of the aggregation requirement in Example No. 7 of *bona fide* hedging positions for physical commodities in Appendix C to the 2013 Position Limits Proposal to eliminate any implication that two persons who enter into a bilateral Referenced Contract, which at least one party hedges with another Referenced Contract, are required under proposed CFTC Rule 150.4 to aggregate their positions solely as a result of either the bilateral agreement or any hedge that either party may enter into to manage the price risk associated with the bilateral agreement.[9]

- Information sharing for risk management purposes. The Commission should clarify that an exemption from aggregation is available to entities that share trading and position information only for risk management purposes even if such information is shared on a real-time basis.

- Disaggregation of majority-owned affiliates. The Commission should permit the disaggregation of majority-owned affiliates which demonstrate that their trading decisions and positions are subject to independent control and management regardless of whether the entities seeking the exemption are required to consolidate their financial statements under U.S. generally accepted accounting principles ("GAAP").

- Disaggregation by registered broker-dealers. The Commission should permit registered broker-dealers to disaggregate *any* ownership or equity interest predicated on the ownership of securities acquired in the normal course of business as a dealer, provided that the broker-dealer does not have actual knowledge of the trading decisions and positions of the owned entity.

- Disaggregation of transitory ownership or equity interests, such as those acquired through foreclosure or a similar credit event. The Commission should adopt a new exemption from the aggregation requirement for banks and other financial institutions holding a transitory ownership or equity interest in an independently controlled entity that was acquired through foreclosure or any similar credit event.

- Information-sharing exemption. The Commission should allow entities relying on the information-sharing exemption to protect their privileged attorney-client communications and confidential work-product by giving them the option to submit a summary explanation of the legal restrictions against sharing information *in lieu* of a full memorandum, provided that they make the full memorandum available for inspection by the Commission or CFTC Staff, upon request.

- Safe harbor period for notice filings. The Commission should provide a safe harbor period for notice filings that are received within a reasonable period of time – up to 180 days – after aggregation is required for entities that otherwise would qualify for

[9] 2013 Position Limits Proposal at 75837.

an exemption. In addition, the Commission should clarify that, provided that a person is otherwise in compliance with the CFTC's position limits rules, an inadvertent failure timely to submit a disaggregation notice would constitute a single violation of the notice requirement in proposed CFTC Rule 150.4(c) and not a daily violation of the underlying position limits in proposed CFTC Rule 150.2.

- *Pro rata* aggregation. The Commission should permit entities to aggregate the positions of an owned entity on a *pro rata* basis, in proportion to their ownership or equity interest. If the Commission does not permit *pro rata* aggregation of an entity's positions in Referenced Contracts, it should *not* require *pro rata* aggregation of cash market positions while simultaneously requiring *full* aggregation of an entity's Referenced Contract positions, as is suggested in the 2013 Position Limits Proposal.

In addition, separate and apart from its substantive comments, FIA is concerned that its members, their affiliates, and other market participants will not have sufficient time to comply with the requirements of the Aggregation Proposal, as it may be modified, based upon the Commission's consideration of public comments. FIA's members experienced an almost identical situation as they, along with all other market participants, struggled to implement the aggregation requirements in the Commission's 2011 Position Limits Rule within the brief transition period provided.

The 60-day transition period provided in the 2011 Position Limits Rule – the *minimum* period permitted under the statute – did not provide enough time for market participants to identify affiliates subject to the aggregation requirements in the final rule (applied for the first time to swaps positions), develop and adopt appropriate policies and procedures, implement necessary information technology systems, and prepare and make the required notice filings to qualify for any applicable exemptive relief. Market participants cannot rationally expend scarce resources preparing to implement a proposed aggregation rule that likely will be modified before the Commission issues a final rule. Accordingly, FIA respectfully requests that the Commission exercise its discretion to provide market participants with a reasonable transition period comprised of: (1) an effective date 60 days after the final rule is published in the Federal Register; and (2) a compliance date nine months after the effective date. FIA submits that this reasonable transition period, rather than the 60-day statutory minimum, is necessary to enable market participants to comply with the requirements in the final rule without incurring unnecessary costs and disruption to their ongoing business.

III. FIA's Comments

A. The Commission Should Affirm that Aggregation Pursuant to an Express or Implied Agreement Is Required Only when the Parties Agree to Trade Referenced Contracts Pursuant to Such an Agreement

Section 4a(a)(1) of the CEA provides, in part, that "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."[10] The plain language of section 4a(a)(1) of the CEA requires two persons who agree, explicitly or implicitly, to a common trading or position management strategy to aggregate their positions for purposes of complying with the CFTC's position limits rules. It manifestly does *not* require two persons who enter into a bilateral Referenced Contract to aggregate their positions solely as a result of either: (1) that agreement; or (2) any hedge, in either a Referenced Contract or a contract subject to exchange-set limits, that either of them may enter into to manage the price risk associated with the initial agreement.

Appendix C of the 2013 Position Limits Proposal includes 14 examples of *bona fide* hedging positions for physical commodities.[11] Example No. 7, which is based on the following fact pattern, includes comments about aggregation that FIA respectfully submits are incorrect:

> 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. In return for the farmer entering into the fixed-price forward sale, *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 reduces the farmer's downside price risk associated with his anticipated agricultural production. The Sovereign faces commodity price risk as it stands ready to pay the farmer the difference between the market price and the price of the fixed-price contract. 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.[12]

The agreement by the Sovereign to pay the farmer the difference between the market price at the time of harvest and the price of the fixed-price forward is, in effect, a swap between the Sovereign and the farmer. Consistent with prudent and common risk management practices, the Sovereign then enters into a separate agreement to manage the risk it incurs on the swap with the farmer.

In its analysis of Example No. 7, the Commission states without elaboration that "[b]ecause the Sovereign and the farmer are acting together pursuant to an express agreement, the aggregation provisions of § 150.4 apply and they are treated as a single person for purposes of position limits."[13] The Commission does not identify the express agreement. Thus, the only

---

[10] CEA section 4a(a)(1) (emphasis added).

[11] 2013 Position Limits Proposal at 75835-39.

[12] *Id.* at 75837.

[13] *Id.*

apparent candidate is the swap between the Sovereign and the farmer, an agreement that is no different than any other bilateral swap between two independent legal entities.

FIA believes that the Commission's application of the aggregation requirement in proposed CFTC Rule 150.4 to this fact pattern is incorrect and inconsistent with the Commission's precedent.[14] None of the transactions described in Example No. 7 are "an expressed or implied agreement or understanding" through which the Sovereign and farmer have agreed to coordinate their positions or trading. On the contrary, both transactions in Example No. 7 – the swap with the farmer and the Sovereign's hedge – are arm's-length agreements that establish distinct, independent positions. In order for the Sovereign and farmer to trade "pursuant to an expressed or implied agreement or understanding," they would need, at a minimum, to reach an understanding about coordinating their trading strategy and position management. There is no indication in Example No. 7 that the Sovereign and the farmer ever even discussed, much less agreed on, whether to buy or sell a Referenced Contract, the size, price and term of any transaction, or how to manage any resulting position. Indeed, a bilateral transaction between independent counterparties is the antithesis of an express or implied understanding to coordinate trading and position management. In a bilateral transaction, the parties agree to take *opposite positions* and, if they elect to hedge those positions, their hedges will be in opposite directions. Moreover, in this example, the issue of whether the Sovereign elects to hedge the exposure from the swap is irrelevant to the farmer's decision to enter into their bilateral transaction.

For all of these reasons, FIA requests that the Commission revise or delete the discussion of the aggregation requirement in Example No. 7 in Appendix C to the 2013 Position Limits Proposal to eliminate any suggestion that common, bilateral transactions may constitute "acting together pursuant to an express [or implied] agreement," which would thereby trigger the aggregation requirement in proposed CFTC Rule 150.4.[15]

---

[14] In *In re* Volume Investors Corp. [1990-1992 Transfer Binder], Comm. Fut. L. Rep. (CCH) ¶ 25,234 (Feb. 10, 1992), the Commission held that the respondents were required to aggregate their positions because their "course of conduct" demonstrated that an implied agreement or understanding existed. *Id.* at 38,677-78 (citation omitted)(internal quotation marks omitted). The Commission identified the following factors, none of which appears to apply to Example No. 7, as relevant to the determination of whether an agreement or understanding exists: "(1) common trading patterns or strategies; (2) common business, financial, and social relationships; (3) common access to account and trading information; (4) common financing, *e.g.*, money transfers and low interest loans, etc.; (5) common brokerage firms; (6) common record keeping; (7) relative inexperience of one or more traders; and (8) family relationships." *Id.* at 38,677. None of these factors provides support for characterizing an arm's-length bilateral transaction as an "agreement or understanding" within the meaning of section 4a(a)(1).

[15] 2013 Position Limits Proposal at 75837.

B. The Commission Should Adopt, with FIA's Recommended Clarifications and Amendments, the Proposed Aggregation Exemption for All Independently Controlled and Managed Owned Entities

As FIA has commented previously, requiring market participants to aggregate all positions of owned entities in which they have a 10 percent or greater ownership interest, even if the owned entities trade and manage their positions independently, is not necessary to achieve the Commission's policy objectives and is commercially impracticable for many FIA members, their affiliates, and other commercial companies. The Aggregation Proposal appropriately provides companies with the opportunity to rebut a presumption that a 10 percent ownership interest establishes actual control over the trading of Referenced Contracts using one of two general methods: (1) a streamlined process that is effective upon filing for minority-owned entities that share no more than 50 percent common ownership; and (2) a more rigorous process that requires prior Commission approval for majority-owned entities.

Under both processes, the entities seeking relief from the aggregation requirement must be independently managed and controlled. To demonstrate such independence, the entities must have in place certain structural and operational controls that include, among other things, measures to ensure that the persons who control the trading of each entity: (1) do not have knowledge of the trading decisions and positions of the other; and (2) trade pursuant to separately developed and independent trading systems.

1. The Commission Should Clarify that Sharing Information Solely for Risk Management Purposes Is Permitted by the Exemption from Aggregation

The Aggregation Proposal states that, although knowledge of trading decisions of an owned entity may raise concerns about independence and the risk for coordinated trading, those concerns do not arise with respect to "information sharing solely for risk management, accounting, compliance, or similar purposes and information sharing among mid- and back-office personnel that do not control, direct or participate in trading decisions."[16] Moreover, the Commission explained in connection with the 2012 Aggregation Proposal that it "does not consider knowledge of overall end-of-day position information to necessarily constitute knowledge of trading decisions, so long as the position information cannot be used to dictate or infer trading strategies."[17] According to the Commission, "knowledge of end-of-day positions for the purpose of monitoring credit limits for corporate guarantees does not necessarily constitute knowledge of trading information."[18] Nevertheless, the Commission noted that "the ability to monitor the development of positions *on a real-time basis could constitute knowledge*

---

[16] Aggregation Proposal at 68961.

[17] *Id.* at 68961 n.122; *see also* 2012 Proposed Aggregation Rule at 31774.

[18] Aggregation Proposal at 68961 n.122; 2013 Position Limits Proposal at 75837.

of trading decisions because of the substantial likelihood that such knowledge might affect trading strategies or influence trading decisions of the other."[19]

FIA generally supports this proposed guidance, including the guidance provided in connection with the 2011 Position Limits Rule which, for the sake of minimizing regulatory ambiguity, FIA requests that the Commission incorporate into the final rule.[20] The Aggregation Proposal appropriately excludes aggregated trading data, such as end-of-day reports and knowledge of trading decisions used for risk management purposes, from the general rule prohibiting the sharing of trading information. However, the Commission should clarify that sharing such information among risk managers, even on a real-time or on-demand basis, also is consistent with the exemption, provided that it is done solely for the purpose of monitoring credit limits or for other risk management purposes. Without this clarification, the Aggregation Proposal may inadvertently limit beneficial and prudent risk management activities.

2. The Commission Should Clarify that the Exemption from Aggregation Is Available for Any "System" that Does Not Enable Coordinated Trading

The Commission clarifies in the Aggregation Proposal that "'separately developed and independent trading systems'" would not necessarily "prevent an owner and an owned entity from both using the same 'off-the-shelf' system" developed by a third party.[21] Rather, because the Commission's primary concern focuses on the potential for coordinated trading, not the trading system itself, the use of any particular technology would not disqualify either entity from relying on an exemption from aggregation, provided that the product or service is not used by multiple parties to share their positions or trading information.[22]

FIA supports this proposed guidance. However, FIA requests that the Commission clarify that this guidance applies equally to all other technologies related to trading, including products and services that are not necessarily labeled as "trading systems" in the ordinary course, such as execution systems that facilitate the booking and confirmation of orders and other back office programs that support an entity's trading operations. As with "off-the-shelf" trading systems, other common (or even shared) technologies that do not enable multiple users to share trading or position information do not create the potential for coordinated trading activity and, therefore, should fall within the scope of the exemption from aggregation.

In addition, the Commission should clarify that its guidance is not limited to systems or other technologies developed by third parties. Many large institutions develop their own proprietary trading software. This is particularly true where programs are needed to support

---

[19] Aggregation Proposal at 68961 n.122 (emphasis added).

[20] 2012 Proposed Aggregation Rule at 31774.

[21] Aggregation Proposal at 68961-62.

[22] *Id.*

transactions involving new and complex products for which there may be no practical third-party software solutions. In certain circumstances, this technology may be sold or licensed to affiliated entities. Provided that these internal systems are not used to coordinate trading, they should be eligible for the exemption from aggregation.

3. The Commission Should Adopt the Exemption from Aggregation for Majority-Owned Entities without Regard to Whether the Entities Seeking to Disaggregate Are Required to Consolidate Their Financial Statements

The Aggregation Proposal includes an exemption from the aggregation requirement for certain majority-owned entities provided that, among other things: (1) the entity seeking to disaggregate its positions can demonstrate that it does not control the trading of the owned entity; and (2) both the person and the owned entity have procedures in place that are reasonably effective to prevent coordinated trading. Unlike other exemptions in the Aggregation Proposal, including the exemption for certain minority-owned entities, the exemption for majority-owned entities would be effective only *after* review and approval by the Commission. However, as proposed, the exemption from aggregation would be available only for certain majority-owned entities that are not required to, and that do not, prepare consolidated financial statements under GAAP, regardless of whether the two entities demonstrate that their trading activities and positions are independently managed and controlled.

FIA strongly supports the inclusion of an exemption from the aggregation requirement for certain majority-owned entities. However, FIA requests that the Commission amend the Aggregation Proposal to allow *all* majority-owned entities, including majority-owned entities that prepare consolidated financial statements, to rebut the presumption of control solely by demonstrating that they do not control the trading and positions of the owned entity through, among other things, effective procedures that prevent coordinated trading. The requirement to consolidate financial statements is, as the Commission notes, based upon accounting principles that are wholly unrelated to the question of actual control of day-to-day trading decisions and positions. Arbitrarily limiting the exemption to entities that are not required to prepare consolidated financial statements would make an important exemption from an onerous regulatory requirement unavailable to many majority-owned entities that, in all other ways, conduct their trading activities in a fully independent manner.

Moreover, because the exemption for majority-owned entities would be effective only after a Commission determination, the Commission retains discretion to determine, on a case-by-case basis, whether the exemption should be granted. FIA's pragmatic recommendation avoids the need to impose arbitrary outcomes on market participants based upon an abstract numeric threshold by providing the Commission with flexibility to evaluate and accommodate the various corporate structures and relationships that exist among FIA members in a manner that is consistent with the CEA and the Commission's policy objectives.

The Aggregation Proposal also requires "each representative (if any) of the . . . board of directors (or equivalent govern[ing] body)" of a majority-owned entity seeking an exemption from the aggregation requirement to certify "that he or she does not control the trading decisions

of the owned entity."[23] FIA suggests that the Commission remove this condition from the final rule. The involvement of a member of a majority-owned entity's board of directors in the trading decisions of that entity has no bearing on the question of whether the trading and positions of majority-owned entity and its parent company are independently managed and controlled. Imposing an additional regulatory requirement on majority-owned entities that is unrelated to the risk of coordinated trading creates additional and unnecessary compliance costs and burdens for market participants.

C. Registered Broker-Dealers Should Be Permitted to Disaggregate Any Ownership or Equity Interest that Is Predicated on the Ownership of Securities Acquired in the Normal Course of Business as a Dealer

The Aggregation Proposal provides an exemption from the aggregation requirement for the accounts of an owned entity where the ownership or equity interest is based on participation in the distribution of securities by an issuer or through an underwriter.[24] Notably, the Commission would *not* limit the availability of the aggregation exemption for issuers and underwriters to circumstances where the relevant ownership or equity interest in the owned entity is 50 percent or less.

The Aggregation Proposal also provides an exemption from the aggregation requirement for an ownership or equity interest by a registered broker-dealer that is acquired in the dealer's normal course of business. However, in contrast to the exemption for issuers and underwriters, the exemption for registered broker-dealers is available only where the ownership interest is equal to 50 percent or less.[25] Rather than explain this disparate treatment of issuers and underwriters compared to broker-dealers, the Commission simply concludes that "a greater than 50 percent ownership interest in an owned entity (other than in a distribution of securities directly by an issuer or through an underwriter) requires aggregation, and further relief from this requirement is not appropriate."[26]

FIA recommends that the Commission permit broker-dealers to rely upon the exemption from aggregation regardless of whether the broker-dealer's ownership or equity interest in an owned entity exceeds 50 percent, provided that the broker-dealer does not have actual knowledge of the trading decisions and positions of the owned entity. The rationale behind providing the exemption extends to *all* situations where a broker-dealer acquires an ownership interest as part of its brokering or dealing activities in the normal course of business. There is no rational basis for distinguishing between underwriting and dealing in securities. In both circumstances, the ownership interest will be temporary and, therefore, will not implicate the independence of the owned entity's trading activity. Accordingly, there is no need to impose an ownership

---

[23] *Id.* at 68977.

[24] *Id.* at 68964.

[25] *Id.*

[26] Aggregation Proposal at 68964.

aggregation requirement in connection with *either* underwriting activity or traditional broker-dealer services.

D. The Commission Should Adopt an Exemption from Aggregation for Transitory Ownership or Equity Interests

Many commercial financing agreements are supported by collateral in the form of a lien on the assets or pledge of the equity of either the debtor or a third-party company. In these agreements, upon an event of default, the creditor may obtain the ownership or equity interest "in satisfaction of a debt previously contracted" as the collateral passes from the debtor to the creditor. In virtually all cases, the creditor then would seek to divest this equity interest in the most orderly, expeditious, and economical manner possible – the equity interest is not held for the purpose of managing the company or its trading. However, in the interim, because title to the collateral may pass by operation of law and without any contemporaneous notice to the affiliated entities that potentially would be affected, an entity subject to position limits may have no actual knowledge, and no reasonable ability to know, that it is required to aggregate with a new, temporary affiliate.

Although the Aggregation Proposal includes exemptions from the aggregation requirement for certain activities commonly engaged in by financial institutions (*i.e.*, underwriting, broker-dealer activities), there is no equivalent exemption or guidance regarding a transitory ownership or equity interest acquired through foreclosure or a similar credit event. As a result, a creditor that obtains a 10 percent or greater ownership or equity interest in another entity that holds positions in futures, options, or swaps immediately will become subject to the aggregation requirement regardless of whether it has knowledge of the new ownership or equity interest, even though the relationship is temporary and focused on realization of the collateral, and without control of any trading decisions. Although this may not be a common occurrence, without a narrowly tailored exemption from the aggregation requirement, a market participant that acquires a transitory ownership or equity interest in another entity through foreclosure or a similar credit event may inadvertently violate the position limits rules even though it has no reasonable means of complying with this requirement.

FIA requests that the Commission adopt an exemption from aggregation for transitory ownership or equity interests in an owned entity, such as those acquired through foreclosure or a similar credit event.[27] Consistent with the exemptions for underwriting and regulated broker-dealer activities, market participants should, subject to the same limited conditions, be permitted to disaggregate such a temporary ownership or equity interest in an independently controlled entity without providing prior notice to the CFTC because, in many cases, prior notice may not be possible. Moreover, because the collateral may involve a company that has recently experienced a default or similar credit event, this exemption should be valid for a commercially

---

[27] *See* Attachment A, *infra*, for proposed language.

reasonable period of time to enable market participants to liquidate the ownership or equity interest in an economical and non-disruptive manner.

E. The Commission Should Modify the Exemption for Information-Sharing Restrictions to Require Market Participants to Make a Memorandum of Law Available Only upon Request

In the Aggregation Proposal, the Commission suggested a revised exemption for information-sharing restrictions which provides that a market participant is not required to aggregate "positions or accounts of an owned entity if the sharing of information associated with such aggregation . . . creates a reasonable risk that either person could violate state or federal law or the law of a foreign jurisdiction, or regulations adopted thereunder . . . ."[28] The exemption is available only for market participants who do not have actual knowledge of the trading and positions or accounts of the owned entity *and* who have filed a notice and memorandum of law prior to relying on the exemption. In previous versions of this rule, the Commission had required an *opinion of counsel* concluding that there was an *actual* violation of federal law or regulation in order for this exemption to apply.[29]

FIA supports the Commission's refinement of the proposed information-sharing restriction exemption from previous iterations of the rule. Specifically, FIA supports the provisions that permit: (1) market participants to prepare a memorandum of law, rather than a formal opinion of counsel, in support of their conclusion that the sharing of information could create a reasonable risk of violating federal, state, or foreign law, or any regulations thereunder; and (2) the memorandum of law to be prepared either by internal or external counsel, and "in a general manner" by a group of similarly situated market participants, rather than individually by every market participant to which the exemption would be available. These are sound commercially reasonable policy adjustments that have eased FIA's concerns regarding the financial, administrative, and temporal constraints that prior versions of the rule would have imposed upon FIA members.

The Commission should further mitigate the burdens associated with the Aggregation Proposal, without compromising its regulatory objectives, by permitting entities relying on this exemption to submit to the Commission a summary explanation of the legal restriction against sharing information, *in lieu* of a full memorandum. This modification would allow market participants to protect their privileged attorney-client communications and confidential work-product without limiting the Commission's ability to ensure that the exemption is being applied correctly because the full memorandum would remain available for inspection by the Commission or CFTC Staff, upon request.

---

[28] Aggregation Proposal at 68977.

[29] 2011 Position Limits Rule at 71693 ("Provided, however, that such person file a prior notice with the Commission detailing the circumstances of the exemption and an *opinion of counsel* that the sharing of information *would cause* a violation of Federal law or regulations adopted thereunder.") (emphasis added).

F. Market Participants Should Be Permitted to Rely upon an Aggregation Exemption for a Reasonable Period of Time before Filing a Disaggregation Notice

The Aggregation Proposal provides that a market participant seeking an exemption must file a notice with the Commission *prior* to disaggregating its positions, even if it would have been eligible to rely on the exemption, but for the notice requirement. FIA requests that the Commission allow for a 180-day safe harbor period during which time a market participant could rely upon an exemption for which it is otherwise eligible, prior to submitting the requisite notice filing to the Commission. In addition, FIA requests that the Commission clarify that, provided that a person is otherwise in compliance with the CFTC's position limits rules, an inadvertent failure timely to submit a disaggregation notice would constitute a single violation of the notice requirement in proposed CFTC Rule 150.4(c) and not a daily violation of the underlying position limits in proposed CFTC Rule 150.2.

When a large and complex corporate entity acquires a 10 percent or greater ownership or equity interest in another entity, it may take time to determine whether the acquired entity directly or indirectly holds positions in Referenced Contracts that are subject to aggregation. Although sharing such information may be relatively simple in some circumstances, in many other cases it likely will be very difficult to establish the necessary protocols to ensure timely compliance with the aggregation requirement. This is particularly true where the acquisition involves a *minority* interest in an entity that only *indirectly* holds positions in Referenced Contracts.

A time-limited safe harbor with the clarifications requested above would reduce the regulatory uncertainty and potential liability that may arise in circumstances where an entity becomes subject to the aggregation requirement before it has knowledge of, or the ability to comply with, the requirement. Moreover, providing such a safe harbor only to entities that would otherwise qualify for an exemption from aggregation would allow market participants the necessary time to come into compliance with the rule without imposing potentially unworkable administrative burdens and without tolling other applicable regulatory requirements.

G. Market Participants Should Be Required to Aggregate Positions Only *Pro Rata*, Based on Their Percentage Ownership of an Owned Entity

1. Pro Rata Aggregation

The Aggregation Proposal states that "all positions in accounts for which any person . . . directly or indirectly controls trading or holds a 10 percent or greater ownership or equity interest must be aggregated with the positions held and trading done by such person."[30] Under current rules, a person must aggregate 100 percent of the positions of an owned entity regardless of

[30] Aggregation Proposal at 68976.

whether the person has a 10, 25, 50, or 100 percent ownership interest. The absence of a *pro rata* apportionment of positions results in the same position being counted toward the CFTC's limits multiple times by multiple entities. Full attribution to a parent company of the positions of an owned entity unnecessarily restricts the ability of market participants to trade and manage their risk effectively, reduces market liquidity, and provides the Commission with data that overstates the actual positions of market participants.

FIA recommends that the Commission revise the Aggregation Proposal so that where aggregation is required on the basis of ownership, market participants will have the option to aggregate the positions of an owned entity on a *pro rata* basis.[31] Although FIA submits that aggregation based on control, rather than ownership, is the most effective way to implement position limits, if the Commission requires aggregation regardless of control, it should allow a market participant to aggregate the positions of an owned entity in proportion to its ownership interest therein (*e.g.*, Company A should be permitted to aggregate 75% of the positions of Affiliate B where Company A owns 75% of Affiliate B). A *pro rata* approach to aggregation would: (1) more accurately reflect the positions owned by market participants; and (2) ensure that the Commission does not unnecessarily restrict the positions of market participants and, thereby, adversely affect the liquidity of Referenced Contracts. Moreover, because every position would be counted under a *pro rata* approach to aggregation, FIA's recommendation would not pose any increased risk of excessive speculation or manipulation.

2. The Commission Should Not Limit the Ability of Aggregated Entities to Hedge the Cash Market Positions of Their Affiliates

In the 2013 Position Limits Proposal, the Commission informed the public that it planned to retain its current practice of treating entities required to aggregate accounts or positions as "the same person when determining whether they are eligible for a *bona fide* hedging position exemption."[32] As a result, when one entity owns 10 percent or more of another entity, it is required to aggregate *all* of the owned entity's positions with its own positions, unless an exemption from aggregation applies.

Notwithstanding the Commission's clear and longstanding practice regarding the treatment of futures (and now swaps) positions of aggregated entities, the 2013 Position Limits Proposal appears to take an inconsistent approach with respect to related cash market positions of aggregated entities. In a footnote, the Commission "clarifies" when it would be economically appropriate for one entity to offset the cash market risk of an affiliate, stating that "[i]t would *not* be economically appropriate for an entity to offset all the risk of an affiliate's cash market exposure unless that entity held a 100 percent ownership interest in the affiliate. For less than a 100 percent ownership interest, *it would be economically appropriate for an entity to offset no*

---

[31] *See*, *e.g.*, 2011 Position Limits Rule at 71704 (Appendix 4, Statement of Commissioner Scott O'Malia).

[32] 2013 Position Limits Proposal at 75736.

more than a pro rata amount of any cash market risk of an affiliate, consistent with the entity's ownership interest in the affiliate."[33]

If the Commission declines to permit *pro rata* aggregation of positions in Referenced Contracts, but requires *pro rata* aggregation of the underlying cash market positions, it will limit the ability of aggregated entities to hedge the cash positions of their affiliates. For example:

- Company A owns 51 percent of Company B.
- Company A has entered into fixed-price contracts to sell 3 million bushels of soybeans, which it has hedged with 600 futures contracts.
- Company B has entered into fixed-price contracts to sell 12 million bushels of soybeans, which it has hedged with 2,400 futures contracts.
- The position limit for soybeans is 600 contracts.

Absent an exemption from the aggregation requirement, Company A would be required to aggregate its positions with the positions of Company B, so that Company A would have an aggregate position of 3,000 futures contracts. Because the spot month position limit for soybeans is 600 contracts, Company A would need to demonstrate that at least 2,400 contracts qualify as *bona fide* hedging positions. If the cash market positions of Company A and Company B are aggregated in the same manner as their Referenced Contracts, Company A's futures positions will qualify as *bona fide* hedging positions because they hedge a corresponding quantity of a cash commodity sales contracts. However, if Company A is permitted to offset only 51 percent of Company B's cash market exposure (*i.e.*, 1,224 contracts), it automatically would exceed the applicable position limit even though *every contract* qualifies as a *bona fide* hedging position.[34] The only way for Company A and Company B to avoid this violation and still hedge their *bona fide* commercial risk would be for Company B to hedge its risk through Company A and the other entities that hold the remaining 49 percent ownership or equity interest, even though these minority owners may be numerous and entirely passive.

---

[33] *Id.* at 75736 n.450 (emphasis added).

[34] Company A would have an aggregated futures position of 3,000 contracts (Company A's 600 contracts + Company B's 2,400 contracts), and an aggregated cash position of 1,824 contracts (Company A's fixed-price contracts to sell 3 million bushels + 51 percent of Company B's fixed-price contracts to sell 12 million bushels = 9.12 million bushels or 1,824 futures equivalent contracts).

	Company A	**Company B (51% owned by Company A)**
CBOT Soybeans (ZS) Spot Month Position Limit	600 contracts	
Soybeans Cash Position	3 million bushels (short)	12 million bushels (short)
CBOT Soybeans (ZS) Hedge	600 contracts (long)	2,400 contracts (long)
Under the Aggregation Proposal and 2013 Position Limits Proposal		
Actual Aggregated Cash Position	15 million bushels (short) (3 million bushels from Company A + 12 million bushels from Company B)	N/A
***Pro Rata* Aggregated Cash Position**	9.12 million bushels (short) (3 million bushels + 51% of 12 million bushels)	5.88 million (short) (attributed to the 49% owners)
Maximum Permitted Hedge	2,424 contracts (long) (equal to 1.212 million bushels) (600 contract position limit + 3 million bushels + 51% of 12 million bushels)	N/A
Aggregated Position in Referenced Contracts	3,000 CBOT Soybeans (ZS)	
***Bona Fide* Hedging Positions Subject to Position Limits in Violation of CEA section 4a(c)(1)**	576 contracts in excess of the applicable limit	

The plain language of section 4a(c) of the CEA provides that "[n]o rule, regulation, or order issued under subsection (a) of this section shall apply to transactions or positions which are shown to be *bona fide* hedging transactions or positions, as such terms shall be defined by the Commission by rule, regulation, or order consistent with the purposes of this Act."[35] This prohibition against limiting *bona fide* hedging has been a part of the CEA since its enactment in 1936.[36] To ensure that, consistent with the plain language of the CEA, all aggregated market participants remain able to hedge effectively 100 percent of their aggregated *bona fide* cash market exposure, the Commission must either permit *pro rata* aggregation of positions in Referenced Contracts, or revise the 2013 Position Limits Proposal so that cash market and Referenced Contract positions are treated in the same manner when applying aggregation requirements.

---

[35] CEA section 4a(c).

[36] Commodity Exchange Act of 1936, ch. 545, section 4a(3), 49 Stat. 1491, 1493 ("No order issued under paragraph (1) of this section shall apply to transactions which are shown to be bona fide hedging transactions.").

IV. Conclusion

For the foregoing reasons, FIA respectfully requests that the Commission modify the Aggregation Proposal and Example No. 7 in the 2013 Position Limits Proposal in accordance with FIA's comments and recommendations. Please contact Barbara Wierzynski, Executive Vice President and General Counsel, or Allison Lurton, Senior Vice President and Deputy General Counsel, at 202-466-5460, if you have any questions about FIA's comments or recommendations.

Sincerely,

Walt Lukken
President & Chief Executive Officer

cc: Honorable Mark P. Wetjen, Acting Chairman
Honorable Bart Chilton, Commissioner
Honorable Scott D. O'Malia, Commissioner
Mark Fajfar, Assistant General Counsel
Stephen Sherrod, Senior Economist
Riva Spear Adriance, Senior Special Counsel

ATTACHMENT A

Proposed Exemption from Aggregation for a Transitory Ownership or Equity Interest Acquired Through Foreclosure or a Similar Credit Event

(__) *Exemption for transitory ownership or equity interests acquired through foreclosure or a similar credit event.* A person need not aggregate the positions or accounts of an owned entity if it acquires, in the normal course of such person's business, a transitory ownership or equity interest in the owned entity as a result of a default, foreclosure, or similar credit event, provided that such person does not have actual knowledge of the trading decisions of, and disposes of its ownership or equity interest in, the owned entity within a commercially reasonable period with due regard to the then prevailing circumstances.