ISDA Safe, Efficient Markets

November 12, 2015

Submitted Electronically

Mr. Christopher Kirkpatrick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street NW
Washington, DC 20581

Re: Aggregation of Positions; Supplemental Notice of Proposed Rulemaking (RIN 3038-AD82)

Dear Mr. Kirkpatrick:

The International Swaps and Derivatives Association, Inc. ("ISDA")[1] appreciates the opportunity to submit these comments with respect to the supplemental notice of proposed rulemaking published by the Commodity Futures Trading Commission ("**CFTC**", or the "**Commission**") (the "**Supplemental Proposal**")[2] regarding the proposed revision to the aggregation provisions of part 150 of the Commission's regulations on position limits. We have previously submitted our comments and recommendations on the Commission's proposed rulemakings on position limits and aggregation on several occasions[3] and we stand ready to provide any further assistance in this process that may be of help to the Commission.

1 Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 850 member institutions from 68 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's web site: www.isda.org.

2 *Aggregation of Positions*, 80 Fed. Reg. 58365 (September 29, 2015).

3 ***E.g.***, ISDA/SIFMA Comment Letter re Proposed Regulations Regarding Position Limits for Derivatives, January 11, 2011; ISDA/SIFMA Comment Letter re Notice of Proposed Rulemaking – Position Limits for Derivatives (RIN 3038-AD15 and 3038-AD16), March 28, 2011; ISDA/SIFMA Comment Letter re Position Limits for Futures and Swaps (RIN 3038-

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We appreciate and support the Commission's general approach in the Supplemental Proposal, which we believe will remove much of the uncertainty that market participants will encounter in applying the CFTC's existing aggregation policies. We believe that the Supplemental proposal provides significant clarity regarding the ability to disaggregate one firm's positions from those of certain entities in which the firm may have ownership interests. From a procedural perspective, we similarly support the Commission's efforts to separate the aggregation rulemaking process from the Commission's position limits proposal.[4] We do not believe that the Commission should delay the finalization of aggregation rules until it is also prepared to finalize position limits rules – in fact, market participants cannot fully assess the position limits proposal without first having a complete understanding of the aggregation standards that will apply. Therefore, we recommend that the Commission proceed to adopt final aggregation rules prior to either finalizing or, preferably, seeking further comment on its position limits proposal.

We would like to express our support specifically for the following aspects of the Supplemental Proposal:

1. We support the decision to permit owner entities to claim disaggregation from their owned entities by submitting a notice filing that is effective upon submission to the Commission. As many commenters noted, it would have been an unnecessary administrative burden on both the Commission and market participants, without any corresponding benefit, if the exemption were only available following a Commission review and approval process.

2. We generally support the conditions proposed for the exemption, subject to a few minor comments and requests for clarification, each as set forth in greater detail below. We believe that the Commission's aggregation policies have historically been focused primarily on those relationships wherein one person or entity actually controls the trading strategy and decision-making of another entity. The proposed conditions acknowledge and recognize that this type of control requires much more than a passive ownership interest that one firm may have in another.

As discussed in more detail herein, while we are generally supportive of the Supplemental Proposal, we respectfully request that the Commission:

AD17), January 17, 2012; ISDA Comment Letter re Notice of Proposed Rulemaking – Position Limits for Derivatives (RIN 3038-AD99), February 10, 2014; ISDA/SIFMA Comment Letter re Reopening of Comment Periods – Position Limits for Derivatives (RIN 3038-AD99) and Aggregation of Positions (RIN 3038-82), July 7, 2014.

[4] We understand that the CFTC continues to review the public comments it has received on the position limits proposal, and we note Chairman Timothy Massad's recent statement of September 22, 2015: "As we continue to consider that input and work on a final rule, I want to underscore that the Commission appreciates the importance and complexity of these issues, and we intend to take the time necessary to get it right. We hope to have more to say about issues related to position limits in the coming months." Responding briefly to Chairman Massad's statement, we suggest that if the Commission does intend to continue to pursue a position limits rulemaking, the public and Commission would benefit from the opportunity to first review and, as necessary, provide further comment on a modified and updated version of the original 2013 position limits proposal.

- Clarify that the Supplemental Proposal does not prohibit the sharing of information when used only for risk management and surveillance and other non-trading purposes, such as, for example, information used to assess collateral requirements or verify compliance with applicable credit limits[5] or information maintained by a custodian or other service provider that does not control trading.

- Clarify that there is no presumption of control for trading and aggregation purposes where an owner entity has an ownership interest in an owned entity that is less than 25 percent and does not actually exercise control over trading decisions and strategy of the owned entity, and thus that the exemption and disaggregation notice filing are only required for entities in which an owner maintains an ownership interest of 25 percent or greater in an owned entity.

- Provide that an owner entity filing a notice of trading independence in order to claim an exemption from aggregation under this rule should be required to make subsequent filings only in the event of a change in its compliance with the conditions of the exemption.

I. The Commission Should Clarify that the Supplemental Proposal Does Not Prohibit the Sharing of Information in Certain Situations which Do Not Involve Trading or Trade Decision-making.

As the Commission notes in the Supplemental Proposal, the aggregation requirement focuses on situations where the owner is "able to control the trading of the owned entity."[6] The Commission has also noted that "if the disaggregation criteria are satisfied, the ability of an owner and the owned entity to act together to engage in excessive speculation or to cause unwarranted price changes should not differ significantly from that of two separate individuals."[7] Given the Supplemental Proposal's stated focus on situations which involve control over trading, we believe that the Commission would facilitate compliance by market participants and clarify the scope of the proposed rules by expressly identifying at least two prominent situations where the proposed rules should not apply, which are set forth below.

The Supplemental Proposal Should Not Prohibit the Sharing of Information Used Only for Risk Management and Surveillance Purposes, when Such Information is Not Used for Trading Purposes.

The final condition of the proposed aggregation exemption is that the owner entity and owned entity "do not have risk management systems that permit the sharing of trades or trading strategy."[8] This condition, in our view, is ambiguous and potentially overly

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[5] ***See*** the statement of Commissioner Giancarlo at Appendix 3 to the Supplemental Proposal, 80 Fed. Reg. at 58381.

[6] 80 Fed. Reg. at 58371.

[7] 80 Fed. Reg. at 58371.

[8] 80 Fed. Reg. at 58379.

broad. In particular, it does not specify the types of firms or business units with respect to which "sharing of trades or trading strategy" might be problematic, and could therefore prevent reliance on the exemption by many entities that were intended to be covered, because of uncertainty as to whether they can satisfy this condition. We submit that a complete prohibition on sharing of information is unnecessarily broad and restrictive without any corresponding benefit and will result only in restricting the number of otherwise eligible entities that have sufficient comfort to rely on the exemption. We therefore respectfully request that the Commission expressly clarify, as it did in its 2013 proposal, that:

> "[T]his criterion generally would not prohibit sharing of information to be used only for risk management and surveillance purposes, when such information is not used for trading purposes and not shared with employees that, as noted above, control, direct or participate in the entities' trading decisions. Thus, sharing with employees who use the information solely for risk management or compliance purposes would generally be permitted, even though those employees' risk management or compliance activities could be considered to have an 'influence' on the entity's trading."[9]

In addition to including this guidance expressly in adopting final aggregation rules, we suggest that the Commission include a specific clarification permitting employees at the owner entity, who are not directly or indirectly involved in trading or the supervision of traders, and are prohibited from sharing information with owner entity traders, to receive trading activity and position exposure information of the owned entity – without subjecting the two entities to aggregation requirements.

The real-time processing of risk and exposure-based information is vital to effective enterprise risk management. Owner entities typically need to receive risk and exposure information on an ongoing basis in order to monitor and oversee their investments in owned entities. Owner entities that are unable to monitor their investments are not only likely to be less productive managers, they also potentially risk breaching fiduciary and other duties to their investors.

In the Supplemental Proposal, the Commission has noted that the aggregation requirements are not intended to interfere with longstanding corporate structures.[10] Accordingly, we believe that a specific clarification that the aggregation requirements are not triggered as a result of information sharing for non-trading purposes, such as risk-management or surveillance, would permit the uninterrupted continuance of corporate structures established to facilitate the flow of important information for these purposes. Without this clarification, we submit, entities may be concerned that providing an owner entity with necessary risk management information could be subject to challenge because of the ambiguities in the language in the Supplemental Proposal and such entities might therefore conclude that they cannot rely on the exemption.

[9] 78 Fed. Reg. at 68962.

[10] 80 Fed. Reg. at 58372.

The Supplemental Proposal Should Not Prohibit the Sharing of Information Between Entities Arising from the Use of an Affiliated Service Provider where such Service Provider and its Personnel Do Not Control the Trading of Either Entity.

We also respectfully request that the Commission clarify that the aggregation exemption would be available in circumstances where an owner entity has knowledge of an owned entity's positions by virtue of the owned entity's use of an affiliated service provider, provided that such service provider and its personnel do not control the trading of either entity. It is not unusual, *e.g.*, within a large financial services firm, for an owned entity to use an affiliated futures commission merchant, which serves as clearing member for some of its affiliated entities, or an affiliated custodian, who similarly provides custodial services. Affiliates may also be engaged in support functions that provide access to data regarding an entity's positions, as is the case with affiliates engaged in recordkeeping or reporting information. Similarly, employees within the owner entity and the affiliated service provider may have a role in providing clearing, custodial, or other non-trading services for the owned entity.

In such cases, the affiliated service provider or its employee may have knowledge of the owned entity's positions, which information is necessary to carry out the clearing or custodial services for the owned entity. Where such employee does not also control trading of the owned entity, the Supplemental Proposal's policy concerns regarding coordinated trading activity are not implicated. Accordingly, we believe it would be appropriate and consistent with the Supplemental Proposal, and would significantly assist market participants, if the Commission would clarify that such arrangements involving affiliated service providers will not result in an employee of an owner entity being presumed to have knowledge of, to have gained access to, or to have received data about, trades of the owned entity for purposes of the aggregation exemption.

II. The Commission Should Raise the Threshold Presumption of Control for Trading and Aggregation Purposes to 25 Percent.

In supporting the Supplemental Proposal, Commissioner Giancarlo released a statement inviting "public comment on whether there should be a removal of the presumption of control of an entity for all minority ownership interests[, which] would allow the exclusion now available to minority owners with a stake below 10 percent, while retaining the presumption for interests exceeding 50 percent."[11] We agree with Commissioner Giancarlo's suggestion and support the imposition of a presumption of trading control based on majority ownership – only above which the disaggregation notice filing would be required. If the Commission determines not to adopt a majority ownership threshold for trading control, we believe that raising the threshold for the presumption of trading control to an ownership interest of at least 25 percent would be a significant improvement that could align the Supplemental Proposal with market realities

[11] 80 Fed. Reg. at 58381.

as well as other existing regulatory regimes. In either case, a relationship of actual control would require aggregation, regardless of the level of the ownership interest.

Market realities indicate that 10 percent is too low of a threshold for presuming control.

In our experience, non-majority ownership interests are not typically structured such that the owner entity could (or seeks to) exercise any active level of control over or participation in the owned entities' trading activity. We therefore agree with Commissioner Giancarlo's suggestion that 10 percent is too low of a threshold for presuming control for the purposes of the CFTC's position limits aggregation rules. Accordingly, we recommend that the presumption of control for trading and aggregation purposes, such that a notice filing would be required in order to claim the disaggregation exemption, should not be set at 10 percent.

In particular, we propose that, where one entity has an ownership interest in another entity of, for example, 50 percent or less, such entities should simply not be required to aggregate provided that there is in fact no actual control over trading, coordination of day-to-day management or control, sharing of information, or other factors present that would permit the owner entity to conclude that it could not meet the conditions of the proposed exemption with respect to a given owned entity.

From a practical perspective, we are requesting that the notice filing be required only in those situations where ownership interests are at a level that is historically associated with the practical ability of an owner entity to exercise control over the operational and trading activities of an owned entity. Therefore, and as noted above, we believe that 10 percent is not the appropriate level at which to apply a presumption of trading control. We suggest that majority ownership, or at least 25 percent ownership, would be a far more accurate threshold metric for presumption of control. In this regard, we also observe that a higher threshold of at least 25 percent may significantly reduce the administrative burden on the Commission of receiving and maintaining aggregation exemption notice filings. Further, as we note below, requiring a threshold of at least 25 percent would be more consistent with broader regulatory or statutory approaches.

Several other regulators require an ownership threshold of greater than 10 percent prior to presuming control.

In support of Commissioner Giancarlo's suggestion, we also note that several other statutes and/or regulators utilize a higher ownership threshold than 10 percent in connection with their thresholds for presumptions or attributions of control.

For example, under certain federal banking laws, control is not automatically found until a person or entity holds an ownership interest of 25 percent or more. In particular, Section 2(a)(2) of the Bank Holding Company Act ("BHC Act") provides that:

> "Any company has control over a bank or over any company if—

> (A) the company directly or indirectly or acting through one or more other persons owns, controls, or has power to vote 25 per centum or more of any class of voting securities of the bank or company;
>
> (B) the company controls in any manner the election of a majority of the directors or trustees of the bank or company; or
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> (C) the Board determines, after notice and opportunity for hearing, that the company directly or indirectly exercises a controlling influence over the management or policies of the bank or company."[12]

While this definition and related guidance issued by the Board of Governors of the Federal Reserve System ("Federal Reserve") recognize that control may be exercised by an entity that holds less than a 25 percent ownership interest, we think it is significant that the BHC Act does not formally attribute control based on ownership, assuming there are no other indicia of control present, until a 25 percent ownership threshold is reached. For example, in issuing guidance on this provision, the Federal Reserve has noted:

> "[T]he primary definition of control in the [BHC Act] is based on ownership of 25 percent or more of the voting shares of a banking organization – an amount that does not provide an investor in most cases with complete control over decisions but would allow the investor to play a significant role in the decision making process."[13]

The Federal Reserve permits entities with ownership interests that are less than 25 percent to demonstrate that a control relationship does not exist for BHC Act purposes based on the relevant facts and circumstances.

Similarly, the Investment Company Act of 1940 provides that a person that owns less than 25 percent of the voting securities of a company is presumed not to control such company.[14]

In addition, the CFTC, in the context of its rules governing the interaffiliate exemption from the mandatory clearing requirement, has implemented a majority (*i.e.*, greater than 50 percent) ownership standard for purposes of determining whether entities are "affiliates." In particular, counterparties are eligible for the interaffiliate exemption if, among other things, one counterparty holds a majority ownership interest in the other party.[15]

Like the Federal Reserve, the Securities and Exchange Commission and the CFTC, the Financial Industry Regulatory Authority ("FINRA") also uses an ownership interest of 25

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[12] ***See*** 12 U.S.C. § 1841(a)(2).

[13] ***See*** Policy Statement on Equity Investments in Banks and Bank Holding Companies, Federal Reserve (September 22, 2008).

[14] 15 U.S.C. § 80a-2(a)(9).

[15] 17 C.F.R. § 50.52(a)(1).

percent or more as an indicator of control.[16] FINRA requires its members to file an application for approval following a change in ownership, control or business operation in the form of "direct or indirect acquisitions or transfers of 25 percent or more in the aggregate of the member's assets or any asset, business or line of operation that generates revenues comprising 25 percent or more in the aggregate of the member's earnings measured on a rolling 36-month basis."[17]

We recognize that these ownership thresholds were adopted in different contexts and for different purposes, and therefore may reflect considerations that are not directly applicable to the Commission's aggregation proposal. Nevertheless, each of these thresholds was designed to identify control relationships that would trigger regulatory consequences, and they are therefore relevant to the Commission's further consideration of the aggregation issue. We also note that there is no reason to believe that an owner entity with an ownership interest of between 10 percent and 25 percent in an owned entity automatically and necessarily has sufficient input into or control over the owned entity's trading to warrant aggregation. Of course, if the owned entity actually has such input or control, aggregation would be required under our proposal in any event. Accordingly, we believe that recalibrating the Supplemental Proposal and related Commission guidance to require a threshold of no less than 25 percent would align the Supplemental Proposal more closely with concepts of "control" used by other regulators and statutes.

III. The Commission Should Provide that an Owner Entity is Required to Make Subsequent Filings Only in the Event of a Change in its Compliance With the Conditions of the Exemption.

While we support the proposal to make the notice filing claiming the exemption effective upon submission to the Commission, we also want to respond to Commissioner Giancarlo's specific request for "public comment on whether the Commission should consider modifying the proposed rule to clarify that an owner filing a notice of trading independence in order to claim an exemption from aggregation under this rule need only make subsequent filings in the event of a material change in the owner's degree of control over its subsidiary's positions."[18]

We agree with Commissioner Giancarlo's suggestion. An owner filing a notice of trading independence in order to claim an exemption from aggregation under this rule should be required to make subsequent filings only in the event of a change in its ability

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[16] We note that the 25 percent threshold for presuming control is also used by Federal regulators outside the financial sphere. For example, regulations under the Higher Education Act of 1965 identify the "controlling shareholder" of an SEC-registered publicly-traded corporation as a shareholder who holds or controls through agreement both 25 percent or more of the total outstanding voting stock of the corporation and more shares of voting stock than any other shareholder. ***See*** 34 CFR 600.31(c)(2).

[17] FINRA Rule 1017(a)(3).

[18] 80 Fed. Reg. at 58381.

to comply with the conditions of the exemption. We note that the CFTC has adopted this approach in other contexts—for example, in the case of commodity pool operators claiming exemptions with respect to offerings to qualified eligible persons.[19] Accordingly, we respectfully suggest that the language clarify that a subsequent notice filing is only required:

- when an owner entity is withdrawing the notice filing because it no longer maintains a requisite ownership interest in the owned entity, or
- in the event that the owner entity is no longer in compliance with the exemption criteria with respect to an owned entity or another material change in the contents of the notice filing has occurred.

IV. The Commission Should Clarify Certain Other Aspects of the Notice Filing Process.

We also note that the Supplemental Proposal requires the notice filing to contain a *description of the relevant circumstances that warrant disaggregation*.[20] We are concerned that the Commission may be unlikely to be able to review these descriptions in any meaningful way on an active or real-time basis, given its resource constraints. Further, we note that the Commission will separately retain the authority to request from any entity claiming the exemption information demonstrating that the person meets the requirements for the exemption. Therefore, we would instead respectfully suggest that the notice filing contain only the certification that the entity, as of the date of the filing, meets the conditions of the exemption with respect to each owned entity specified in the filing.

Consistent with the Supplemental Proposal, we agree that the notice filing should be signed or submitted by a senior officer of the owner entity, on behalf of the owner entity.[21] To avoid unnecessary uncertainty, we ask that the Commission clarify that the specific senior officer signing or submitting the notice filing may be any one of a number of individuals, as appropriately determined within the context of a particular owner entity's governance structure.

With respect to timing, we suggest that an owner entity be provided a reasonable amount of time (for example, three months), following the acquisition of an ownership interest in an owned entity that is above the control presumption threshold, in which to conduct the necessary internal review to support and approve the notice filing. That is, aggregation should not be required during the three-month time period following an acquisition or investment but prior to the notice filing deadline. To conclude otherwise would limit and restrict the ability of market participants to make acquisition and investment decisions and would ultimately result in delays in the investment process. However, where an

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[19] ***See*** Rule 4.7(d)(2) under the Commodity Exchange Act.

[20] Proposed rule § 150.4(b)(2)(ii).

[21] Proposed rule § 150.4(c)(1)(ii).

owner entity takes active steps to control and direct the trading strategy of a newly acquired owned entity, aggregation would of course still be required.

We also suggest that the Commission provide for a six-month compliance period, following the effective date of any final aggregation rule, during which entities will be able to undertake the initial diligence and governance processes necessary to support filing for and claiming the owned-entity aggregation exemption with respect to owned entities.

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ISDA appreciates the opportunity to provide these comments. If we may provide further information, please do not hesitate to contact the undersigned or ISDA staff.

Sincerely,

Global Head of Public Policy

cc: Commodity Futures Trading Commission
Timothy G. Massad, Chairman
Sharon Y. Bowen, Commissioner
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