May 14, 2020

VIA ONLINE SUBMISSION

Mr. Christopher J. Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
1155 21st Street, NW
Washington, DC 20581

Re: Position Limits for Derivatives, RIN 3038-AD99

Dear Mr. Kirkpatrick:

CME Group Inc. ("CME Group")[1] appreciates this opportunity to provide comments on the Commodity Futures Trading Commission's ("CFTC" or "Commission") proposal regarding "Position Limits for Derivatives" ("Proposal"), 85 Fed. Reg. 11596 (Feb. 27, 2020).

The Proposal incorporates many of the issues we have addressed in our past comment letters, including, among other things, the need for a finding of necessity before imposing any federal position limit, adoption of non-spot month limits only for the nine legacy agricultural commodities, an exchange-administered process for granting non-enumerated bona fide hedge exemptions, broad application of spread exemptions and spot month limit parity for linked cash-settled and physically-settled markets.

CME Group urges the Commission to finalize the Proposal with certain modifications as outlined below.[2] We believe that adopting our recommendations would better align the Commission's position limits regime with the statutory goals of position limits, including

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[1] CME Group is the parent of four U.S.-based designated contract markets ("DCMs"): Chicago Mercantile Exchange Inc. ("CME"), Board of Trade of the City of Chicago, Inc. ("CBOT"), New York Mercantile Exchange, Inc. ("NYMEX") and the Commodity Exchange, Inc. ("COMEX") (collectively, the "CME Group Exchanges" or "Exchanges"). These Exchanges offer a wide range of products available across all major asset classes, including: futures and options based on interest rates, equity indexes, foreign exchange, energy, metals, and agricultural commodities. CME Group offers futures and options on futures trading through the CME Globex® platform, fixed income trading via BrokerTec and foreign exchange trading on the EBS platform. CME Group also operates CME Clearing, a derivatives clearing organization ("DCO") which provides clearing and settlement services for exchange-traded and over-the-counter derivatives transactions as well as a swap execution facility ("SEF"). With a range of pre- and post-trade products and services underpinning the entire lifecycle of a trade, CME Group also offers optimization and reconciliation services through TriOptima, and trade processing services through Traiana.

[2] Also attached to this letter is an Appendix containing responses to certain specific questions posed in the Proposal.

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preventing excessive speculation, deterring and preventing market manipulation, ensuring sufficient market liquidity for bona fide hedgers and protecting the integrity of the price discovery function of the underlying market.[3]

I. Proposed Federal Speculative Position Limits

CME Group agrees with the Commission's conclusion that it is statutorily required to make a finding that speculative position limits are necessary before imposing any federal limit on any commodity market. As the Commission knows, CME Group has consistently taken the position that it was unreasonable to interpret the Dodd-Frank Amendments to the position limit provisions of the Commodity Exchange Act ("CEA") to mandate that the Commission impose federal limits for all of the physical commodity markets without regard to whether such limits were necessary.[4] Given the importance of federal position limits and the impact they may have on the derivatives markets, Congress has long required a finding that such limits are "necessary to diminish, eliminate or prevent" the burdens of "excessive speculation" before federal limits may be imposed under Section 4a(a)(1) of the CEA. We are pleased the Commission has determined to resolve this issue of statutory interpretation in a manner consistent with the statute's text and the Commission's history and experience.

A. Spot Month Limits are Necessary for the Referenced Contracts; Non-Spot Month Limits are Not.

The Commission has made a preliminary finding that "federal speculative position limits are necessary" for trading **in the spot month** in 25 physical commodity core referenced futures contracts and associated referenced contracts.[5] The Commission also has preliminarily determined that, with the exception of the nine legacy agricultural markets, federal position limits **in the non-spot month** for the balance of the physical commodity reference contracts are not "necessary."[6] CME Group agrees with the Commission's findings and urges the Commission to make them final. CME Group also agrees with the Commission's determination that federal position limits in physical commodity markets other than the 25 specified are not necessary under the Section 4a(a)(1) standard based on existing information and evidence.

CME Group notes that the Commission's Proposal follows the approach to position limits in physical commodity markets adopted by DCMs, including CME Group Exchanges. Applying

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[3] *See* 7 U.S.C. § 6a(a)(3)(B).

[4] *See, e.g.*, Letter from CME Group to CFTC Re: Position Limits for Derivatives, dated March 28, 2011, at 2-7 [hereinafter "2011 Comment Letter"], *available at* https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=33920; Letter from CME Group to CFTC Re: Position Limits for Derivatives (RIN No. 3038-AD99); 78 Fed. Reg. 75,680 (Dec. 12, 2013), dated February 10, 2014, at 5-19 [hereinafter "2014 Comment Letter"], *available at* https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=59718; Letter from CME Group to CFTC Re: Position Limits for Derivatives, RIN 3038-AD99, dated February 28, 2017, at 16-22 [hereinafter "2017 Comment Letter"], *available at* https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=61100.

[5] Proposal at 11664.

[6] Proposal at 11628-29 and 11664 n.459.

our experience, expertise and discretion, and consistent with DCM Core Principle 5, CEA Section 5(d)(5), our Exchanges have concluded that position limits in the spot month are needed for market integrity purposes in markets we operate for cattle, rough rice, gold, silver, copper, platinum, palladium, natural gas, crude oil, heating oil, and gasoline. Our Exchanges have also concluded that position limits in the non-spot months are not necessary for metals and energy contracts; accountability levels and, when warranted, heightened surveillance offer the appropriate level of market integrity protection. We believe these preventative tools for the non-spot month have worked well in our markets and appreciate the Commission's conclusion that accountability levels for the non-spot month have functioned "as an equally robust, yet more flexible, alternative to federal non-spot month speculative position limits."[7] CME Group accordingly recommends that the Commission affirmatively rely on our Exchanges' self-regulatory experience and determinations when finalizing the necessity findings for spot and legacy non-spot month federal position limits.

B. Proposed Definition of Economically Equivalent Swaps

CME Group believes that the definitions of "referenced contract" and "economically equivalent swap" should be consistent to minimize artificial distortions between futures and swaps. Section 4a(a)(5) of the CEA requires the Commission to impose position limits on "swaps that are economically equivalent" to futures if the Commission imposes position limits on such futures. Under the Proposal, federal position limits would apply to applicable referenced futures contracts (and related options) in the 25 physical commodities as well as to "economically equivalent swaps" in those commodities. The Proposal achieves this objective by including "economically equivalent swap" within the definition of "referenced contract."

According to the Proposal, an "economically equivalent" swap must share "identical 'material' contractual specifications with the referenced [futures] contract."[8] The Commission acknowledges that the proposed definition is narrow to prevent parties with large positions in referenced futures contracts from entering into swaps in the same commodity to net down their overall position for limit purposes. That concern is legitimate, but a narrow definition also opens the door to a different risk. As drafted, the Proposal would allow market participants to build up excessive risk exposure on one side of the market or the other, thereby potentially defeating the purposes of the Proposal. For example, a party could increase its risk exposure greatly by holding a position in futures up to the federal limit while holding a position in a closely related swap with the same economic risk profile, doubling up a long or short exposure. The swap, however, would not be subject to the federal limit because a material term of the swap was not identical to the terms of the futures contract.

As we have consistently emphasized in our previous comment letters, CME Group believes that economically and substantively alike contracts should be accorded the same regulatory treatment to prevent artificial distortions from opening doors for manipulators or

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[7] Proposal at 11629.

[8] Proposal at 11615.

shifting one market's liquidity to another.[9] Based on that concern, CME Group believes that the economically equivalent swap and referenced contract definitions should be consistent to remove any disparity between futures and swap markets. In this regard, as noted above, CME Group recommends that the Commission apply similar provisions to both cash-settled and physically-settled swaps. For example, if a physically-settled swap may qualify as economically equivalent even if its delivery date diverges (*e.g.*, by less than one calendar day) from its corresponding physically-settled referenced contract, similar treatment should apply for cash-settled swaps where cash settlement price determination diverges to the same extent from the corresponding cash-settled referenced contract.

The Commission also proposes a slightly broader, special economically equivalent swap definition for natural gas so that swaps with delivery dates that diverge by less than two calendar days—as opposed to less than one calendar day for other swaps—from an associated referenced contract could still be deemed economically equivalent and would be subject to federal limits.[10] Consistent with our position on treating swaps and futures alike for purposes of the referenced contract definition, we believe that parallel treatment of penultimate swap contracts is warranted for other energy futures and swap markets. The Commission's concerns about potential manipulation, regulatory arbitrage and volume shifts in natural gas markets also apply to markets in, for example, crude oil, heating oil and RBOB gasoline. As a result, CME Group believes the Commission should consider potential loopholes that could arise from the narrow definition of "economically equivalent swap" before finalizing the Proposal; expanding that definition may be appropriate.

C. Proposed Position Limit Levels

(i) Spot Month Limit Levels for CME Referenced Contracts Are Appropriate; the 25% of Deliverable Supply Guideline Is a Ceiling, Not a Fixed Formula.

The Commission asked CME Group DCMs to provide recommended federal spot month levels for each of their respective core referenced futures contracts and has proposed to adopt those recommended levels as the federal spot month level. CME Group appreciates the Commission's consideration and careful review of the recommendations we made. We encourage the Commission to adopt those recommended levels in the final rules on federal position limits.

Spot-month limits historically have been set to balance the dual goals of promoting liquidity and preventing delivery month price distortions. To that end, in making our

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[9] *See, e.g.*, 2017 Comment letter, *supra* note 4, at 11-13; Letter from CME Group to CFTC Re: Position Limits for Derivatives: Certain Exemptions and Guidance, RIN 3038-AD99, dated July 13, 2016, at 3-5 [hereinafter "July 2016 Comment Letter"], *available at* https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60926; 2014 Comment Letter, *supra* note 4, at 23-39.

[10] Proposal at 11618.

recommendations, CME Group balanced the needs of bona fide hedgers for robust market liquidity against the risk that a speculator with an excessively large position in the spot month may threaten market integrity and reliable price discovery in the market. In our experience, this balance requires a careful calibration of many factors and the exercise of informed judgment based on regulatory experience and expertise, as the Commission acknowledged in the Proposal.[11] CME Group does not believe in a one-size-fits-all approach to setting spot month position limit levels; we are not aware of any formula that could capture all the nuances and subtleties that attend setting spot month position limit levels.

In making our recommendations to the Commission, CME Group did not plug in 25% of deliverable supply as a magic formula that spits out an answer. Instead, we applied our informed judgment on a commodity-by-commodity basis and recommended that the Commission adopt federal position limit levels that are well below the 25% threshold. We based our recommendations on factors such as contract specifications, market participation, physical market fundamentals, delivery process, convergence, market liquidity, volatility, market participant concentration, and market participant feedback. We do not believe these factors need to be codified in the regulations but rather are criteria to consider when recommending a spot month position limit. For updates on deliverable supply estimates, CME Group believes that DCMs should update deliverable supply estimates every two years; in addition, DCMs should be provided the opportunity to submit data voluntarily to the Commission on a more frequent basis. We believe this is the appropriate approach to spot month levels for DCMs as well as the Commission.

Other DCMs appear to have taken a different path and relied on the 25% of deliverable supply guideline as a fixed formula for establishing recommended limits. CME Group believes that approach is unsound as a matter of policy and incompatible with the Commission's statutory authority to determine that a specific position limit is necessary and set it at an appropriate level. The 25% of deliverable supply guideline has always been understood to be an upper boundary, or ceiling, on the level for position limits in the spot month. Taking an across-the-board approach by setting a federal limit at the full 25 percent of deliverable supply could have a significant negative impact on many markets across all asset classes as we have explained in our prior comment letters.[12] For example, setting a uniform and high federal limit without regard to the unique characteristics of a particular contract market can encourage exchanges to set limits for competitive reasons rather than for regulatory purposes. As the Commission acknowledges, that perverse incentive structure could lead to a race to the bottom and undermine the statutory goals of deterring manipulation and excessive speculation through position limits.[13] For those reasons, CME Group strongly recommends that the Commission not adopt final spot month

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[11] *See* Proposal at 11627 n.199.

[12] *See, e.g.*, Letter from CME Group to CFTC Re: Recommended Federal Spot-Month Limit Levels, dated September 12, 2016 [hereinafter "September 2016 Comment Letter"], *available at* https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=61007.

[13] *See* Proposal at 11696 ("[T]he Commission recognizes that proposed § 150.5(b)(1) could adversely affect market integrity by theoretically allowing DCMs to establish excessively high position limits in order to gain a competitive advantage, which also could harm the integrity of other markets that offer similar products.").

position limit levels at 25% of deliverable supply as a rigid formula and, based on the factors previously described above, work with the exchange to determine an appropriate limit based on the market dynamics previously described.

(ii) Spot Month Limit Parity for Physically-Settled and Cash-Settled Contracts Should Apply Across All Commodity Markets.

CME Group appreciates that the Commission has proposed generally maintaining the same position limits for both physically-settled and cash-settled reference contracts in the same underlying commodity. As noted above, CME Group has long advocated that like contracts be accorded the same regulatory treatment. Otherwise, one side of the market with lower limits could be subject to artificial distortions from potential manipulations on the other side, regulatory arbitrage and liquidity drain to the other side of the market. These distortions would undermine the core statutory goals of position limits, including preventing excessive speculation, deterring and preventing market manipulation, ensuring sufficient market liquidity for bona fide hedgers and protecting the integrity of the price discovery function of the underlying market.[14] Indeed, as CME Group explained at length in prior comments,[15] Congress understood in its enactment of CEA Section 4b (and the CFTC reaffirmed in its implementing regulations) that by using "comparable" limits for cash-settled and physically-delivered contracts, the price discovery process of the linked markets would be protected.[16] Accordingly, CME Group agrees with the Commission's general approach to adopt an even-handed limit for both physically-settled and cash-settled contracts.

CME Group notes that the Commission proposes one exception to this approach for natural gas contracts. CME Group has objected to the proposed conditional spot month limit exemption for natural gas contracts in previous Commission proposals. Any proposed disparity in the spot-month limits could drain liquidity for bona fide hedgers in the physically-settled market and could prevent physical delivery markets from serving the price discovery function that they have long provided. Moreover, we believe that the conditional limit structure could incentivize the manipulation of a cash commodity price in order to benefit a position in a cash-settled contract. For these reasons as well as the reasons stated in our prior comment letters, CME Group objects to any disparities in the spot-month limits and would rigorously disagree if the Commission adopts any other disparities in treatment between physically-settled and cash-settled contracts.

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[14] *See* 7 U.S.C. § 6a(a)(3)(B).

[15] *See, e.g.*, 2017 Comment Letter, *supra* note 4, at 11; September 2016 Comment Letter, *supra* note 12, at 2-4.

[16] *See* 7 U.S.C. § 6(b)(1)(B) (requiring foreign board of trade cash-settled contracts to have "comparable" limits to their linked DCM benchmark futures); 17 C.F.R. § 48.8(c)(1)(ii)(A) (same); *see also* Registration of Foreign Boards of Trade, 76 Fed. Reg. 80674, 80698 (Dec. 23, 2011) (explaining the basis for the comparability requirement).

II. Bona Fide Hedge Exemptions from Position Limits

A. CME Group Supports An Exchange-Administered Process for Recognizing Non-Enumerated Bona Fide Hedge Exemptions.

(i) Proposed Exemption Process

CME Group supports the Commission's proposed new process for exchanges to review and grant bona fide hedge exemptions for purposes of both federal and exchange limits.[17] This streamlined process would wisely leverage exchanges' long history of reviewing hedging approaches and applying those approaches to specific facts and circumstances, and would thereby advance the statutory goal of allowing commercial parties to "hedge their legitimate anticipated business needs" without imposing any undue burden in doing so.[18]

CME Group supports the proposed ten business day period for the Commission to review an exchange's determination to recognize a bona fide hedge as well as the proposed two business day review period for an exchange's approval of retroactive exemption applications. We believe this process would be manageable for the Commission as it is limited to recognizing non-enumerated exemptions. CME Group also agrees that a timeline for exchanges to review applications should not be prescribed. Exchanges often ask follow-up questions or obtain additional information on an original application, and the review process could take longer depending on factors such as the market participant's response time and scheduling issues for meetings. With respect to the Commission's authority under Proposed Rule 150.9(e)(5) to stay pending applications during the ten (or two) business day review period, CME Group believes the Commission's further review period should not extend beyond 30 calendar days to provide certainty to market participants.

CME Group believes that, after an exchange's approval but pending the Commission's ten-day (or two-day) review, the exemption applicant should be permitted to rely on the exchange-granted exemption for purposes of federal position limits. As the Commission acknowledges, exchanges' initial determinations would be based on their experience, expertise, and familiarity with their market participants' commercial needs, practices, and trading strategies.[19] Exchanges also have strong incentives to grant exemptions only after a careful review, as they have statutory responsibilities to prevent manipulation and allow positions to exceed limits only as necessary and appropriate on their markets.[20] Similarly, CME Group believes that pending the Commission's extended review after a stay, the exemption applicant should be permitted to exceed federal position limits under the exchange-granted exemption. If the Commission rejects the exchange's grant of exemption, CME Group believes that, consistent

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[17] *See* Proposed Rule 150.9.

[18] 7 U.S.C. § 6a(c)(1).

[19] *See* Proposal at 11691-92.

[20] *See* 7 U.S.C. § 7(d) (DCM core principles).

with Proposed Rule 150.9(e)(6), the applicant should be permitted a commercially reasonable time to reduce the position to comply with the applicable limit to ensure market orderliness.

CME Group supports Proposed Rule 150.9(e) requiring an exchange to notify the Commission of its initial approval of an exemption application (but not any renewal approvals). We do not believe a notice requirement is necessary for additional review and approval during the renewal process unless there are new material facts and circumstances impacting such review; changes to material facts and circumstances would mean the exemption previously granted would likely no longer apply and require a new exchange approval—which would trigger the requirement to notify the Commission.

(ii) CME Group Recommends Phasing in the Proposed Exchange-Administered Process to Avoid the Concentration of Exemption Applications During a Limited Time Window.

CME Group believes the proposed compliance date of twelve-months after publication of a final federal position limits rulemaking in the Federal Registrar is generally reasonable. We are concerned, however, that the proposed timeline would cause an influx of exemption applications to exchanges near the end of the twelve months, imposing unnecessary burdens every year at the same time. CME Group currently processes over 500 exemptions annually in the contracts subject to the Proposal. Processing all of these exemptions around the same time period could pose unmanageable burdens to the exchange, CFTC staff and Commissioners. Additionally, it would cause uncertainty for market participants if they are delayed in obtaining approval.

CME Group suggests working with the Commission to implement a rolling process where market participants are grandfathered into current exchange approved exemptions they hold today, permitting them to file for those exemptions on the same annual schedule. This may mean starting the proposed exchange-administered process either 6 months prior to the proposed compliance date or extending the compliance date so that a rolling process could commence at a later time. We welcome further dialogue with the Commission to establish a workable process to avoid unnecessary disruption and uncertainty.

B. Proposed Addition to the List of Enumerated Bona Fide Hedge Exemptions

CME Group commends the CFTC for expanding the list of enumerated bona fide hedge exemptions, including anticipatory merchandising.

Additionally, we recommend that the Commission add the hedging of single-sided floating/unfixed-price purchases or sales to the list of enumerated bona fide hedge exemptions. We believe the below example should be enumerated:

> On February 3, 2020, Counterparty X (seller) agrees to deliver 100,000 barrels (100 contracts) of physical WTI crude oil to Counterparty Y (buyer) ratably during the calendar month of March 2020. Counterparty X and Y execute this transaction via a floating/unfixed-priced contract in which the delivery will be priced at the NYMEX March 2020 WTI Crude Oil futures final settlement price on February 20, 2020. Both parties are exposed to floating price risk from contract execution until

pricing; the buyer is exposed to upward price risk to the March 2020 CL futures between February 3 and February 20, and the seller is exposed to downward price risk during this timeframe.

In our view, derivatives positions entered into by Counterparties X and Y to reduce the respective price risk they face under these circumstances would clearly meet the definition of bona fide hedging positions under Proposed Rule 150.1. These positions (1) represent a substitute for transactions to be made at a later time in a physical marketing channel, (2) are economically appropriate to the reduction of price risks in the conduct and management of a commercial enterprise, and (3) arise from the potential change in the value of assets that Counterparty X anticipates merchandising and Counterparty Y anticipates owning.

C. Proposed Elimination of the "Five-Day" Rule

CME Group supports the Proposal's elimination of the five-day rule from enumerated hedging categories.[21] We strongly recommend, however, that the Commission remove the proposed guidance in paragraph (b) of Appendix B regarding positions held during the spot month. Instead, the Commission should allow exchanges to continue to rely on their established market surveillance expertise and regular interactions to make decisions around exemptions.

CME Group believes the proposed guidance could be interpreted to cause unnecessary burden and costs to market participants. The guidance appears to create a formal process for firms to provide information outlined in the Appendix as part of their bona fide hedge exemption applications, but the Proposal does not seem to consider this additional burden in its cost analysis. Today, exchanges have rules in place giving them the authority to ask questions about a market participant's expected use of exemptions and its plans around expiration and ultimately to limit its reliance on the exemption if deemed appropriate. This process has worked well in recognizing exemptions from exchange limits, and we have no reason to believe the same process would not work for recognizing similar exemptions from federal limits. CME Group recommends that the Commission leverage exchanges' existing, well-functioning processes to obviate the need for a market participant to file additional documentation every time it applies for an enumerated bona fide hedge exemption.

Additionally, the proposed guidance could cause further confusion to market participants. For example, it is not clear if the guidance instructs firms to provide these answers on an annual basis or every time they rely on an exemption. It is also not clear if the guidance would apply to all exemption types or only those that previously had been subject to the five-day rule.

D. Retroactive Application for an Exemption

CME Group agrees with allowing participants to file an exemption application up to five days after exceeding a limit under Proposed Rules 150.3 and 150.9. We do not believe, however, that applicants for retroactive exemption should be required to include "an explanation of the circumstances warranting the sudden or unforeseen increases in bona fide hedging

[21] *See* Proposal at 11612.

needs."[22] In our experience, position limit violations often occur unintentionally due to operational or administrative oversight, not because the market participant needed to enter into a hedge quickly in response to changing market conditions. Over the past three years, CME Group has received at least 49 retroactive exemption applications to cure some type of administrative oversight. Additionally, CME Group has not seen the same firm consistently repeating these types of administrative errors.

Further, Proposed Rule 150.5(a)(2)(ii)(A)(*5*) provides that a DCM or the Commission would not consider a person to have violated a position limit even if the application for a retroactive exemption is denied. CME Group disagrees with this approach. Today at the exchange level, CME Group considers firms to be in violation of a position limit if they exceed a limit and the exemption application is denied. We believe the Commission should implement this standard rather than permitting the proposed grace period for denial of an exemption application. Otherwise, market participants with excessively large speculative positions could exploit the grace period accompanying an application for an exemption and intentionally go over the applicable limit without consequences—all the while disrupting orderly market operations. In our experience, the prospect of having an application denied and being found in violation of position limits has worked to deter market participants from attempting to exploit the retroactive exemption process.

E. Requirement of a Factual and Legal Analysis for Bona Fide Hedge Exemption Applications

CME Group recommends removing the requirement for an applicant to provide a factual and legal analysis as part of an exemption application under Proposed Rule 150.3(b)(1)(i)(B). While this proposed requirement may be intended to provide those making the exemption decisions with additional information around the intended hedging strategy, the use of the phrase "factual and legal analysis" could be interpreted to require applicants to have counsel review a description of the hedge and validate its eligibility. CME Group Exchanges have never required applicants to provide detailed legal or economic analysis demonstrating a position's compliance with statutory and regulatory standards. Rather, an applicant must explain its strategy, which the exchange will consider in light of its expertise with the relevant market in performing its own analysis. Requiring an exemption applicant to hire outside counsel to provide a legal analysis could be cost prohibitive as well as impractical from a timing perspective because many market participants need to employ trading strategies in real time. Moreover, exchanges still would be obligated to perform their own analyses of the position's compliance with statutory and regulatory standards. Accordingly, CME Group recommends that the Commission instead require each applicant to explain its strategy and state that it complies with the regulatory requirements for a bona fide hedge exemption without having to provide a legal analysis. If further information is necessary, including a legal analysis, the exchange or Commission could solicit it from the applicant.

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[22] Proposed Rule 150.5(a)(2)(ii)(A)(*3*).

F. Additional Spread Exemptions

CME Group agrees with the inclusion of spread positions in the definition of "referenced contract" under Proposed Rule 150.1. Consistent with our Exchanges' practice today, we further believe a spread that involves a pair of physically-settled and financially-settled positions should be added to the definition, which would include futures and options on futures.[23] Although the Proposal addresses inter-commodity spreads, it does not appear to specifically address this type of spread.

As noted above, CME Group has consistently recommended that the Commission adopt spot-month limit parity for the physically-settled and cash-settled markets. These markets are inherently linked. For example, market participants that hold positions across physically-settled and cash-settled contracts assess their risk profile as though under one combined market, since both types of positions would ultimately settle to the price of the NYMEX physically-settled contract. Allowing spread exemptions for positions covering both settlement types would help maintain liquidity in the physically-settled market during the spot period and assist market participants with managing their risks across linked contracts on multiple venues.

We believe the Commission should also recognize an exchange spread exemption where a market participant is spread two financially-settled markets in the spot period. For example, if a market participant is long the NYMEX Henry Hub Natural Gas Look-Alike Last Day Financial Futures and short the ICE LD1 Fixed Price Future, those positions would net for purposes of the federal limit but the market participant would need an exchange exemption to stay above the applicable exchange limit. In this regard, the Commission has proposed to permit exchanges to grant similar inter-market and intra-market spread exemptions with respect to contracts that would not be subject to the proposed position limits.[24] We believe there is no sound reason to deny exchanges similar authority to grant exemptions for a spread in the identical contract, regardless of whether the contract is subject to federal position limits.

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CME Group appreciates this opportunity to comment on the Proposal and looks forward to continuing its dialogue with the Commission on this important rulemaking. We urge the Commission to adopt the Proposal along with our recommendations provided in this letter. Please contact me with any questions or comments by telephone at (312) 930-3488 or by e-mail at Kathleen.Cronin@cmegroup.com, as well as Thomas LaSala, Managing Director, Chief Regulatory Officer, by telephone at (212) 299-2897 or by e-mail at Thomas.LaSala@cmegroup.com.

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[23] *See* CME Group Rule 559.C Arbitrage and Spread Positions, *available at* https://www.cmegroup.com/content/dam/cmegroup/rulebook/CME/I/5/5.pdf.

[24] *See* Proposal at 11648 (explaining the import of Proposed Rule 150.5(b)(4)).

Sincerely,

Kathleen Cronin
Senior Managing Director, General Counsel
and Corporate Secretary

cc: The Honorable Heath P. Tarbert, Chairman
The Honorable Brian D. Quintenz, Commissioner
The Honorable Rostin Behnam, Commissioner
The Honorable Dawn DeBerry Stump, Commissioner
The Honorable Dan M. Berkovitz, Commissioner
Dorothy DeWitt, Director, Division of Market Oversight
Aaron Brodsky, Senior Special Counsel
Steven Benton, Industry Economist
Jeanette Curtis, Special Counsel
Steven Haidar, Special Counsel
Harold Hild, Policy Advisor
Lillian Cardona, Special Counsel

APPENDIX

- Question (15) Please indicate if any updates or other modifications are needed to: (1) the proposed list of referenced contracts that would appear in the CFTC Staff Workbook of Commodity Derivative Contracts Under the Regulations Regarding Position Limits for Derivatives posted on the Commission's website; or (2) the proposed Appendix D to part 150 list of commodities deemed "substantially the same" for purposes of the term "location basis contract" as used in the proposed "referenced contract" definition.

  Answer: CME Group is hereby supplying as an attachment a proposed list of referenced contracts along with the list of contracts from the CFTC's workbook that we believe should be excluded.

  CME Group believes for commodities with only spot month limits financially-settled futures and options contracts should be excluded from the list of referenced contracts if the final settlement/expiry of the financially-settled future or option occur before the spot month period of its core referenced futures contract begins. In this instance, given the spot month period of the core referenced futures contract has not begun and thus the spot month position limit is not in effect, it does not make sense to include these financially-settled contracts that cash-settle against a non-spot month limit period core referenced futures contract price.

  CME Group also believes option contracts that exercise into physically-settled core referenced futures contracts should be included even if final settlement/expiry of the option occurs before spot month period begins. In this instance, although the option may expire and exercise into a core referenced futures contract before the spot month limit period begins, we think it prudent to include given the participant would still have to manage the underlying futures exposure resulting from the option.

  Finally, CME Group believes all calendar-month average, trade-month average, and balance-of-the-month ("BALMO") contracts should be excluded from the list of referenced contracts and subject solely to Exchange set position limits. In the oil markets in particular a significant amount of commerce is transacted on a monthly average basis and CME Group lists futures and options contracts that settle based off an average of referenced prices over the course of a calendar month, trade month, or BALMO in order to allow commercial participants to hedge their underlying physical market exposure. For example, in the upcoming June 2020 calendar month there are 22 US business days and thus 22 daily referenced prices incorporated into the calendar month average. As such, the final settlement price of a core referenced futures contract in the June 2020 calendar month would be 1/22nd of the final settlement calculation of a corresponding June 2020 calendar month average contract. Further, any OTC swap that settles off a monthly average that would be hedged by a market participant with one of these instruments would not be treated as an economically equivalent swap. Given the pricing convention and risk exposure of these contracts and the CFTC's proposal of economically equivalent swaps, CME Group believes these average pricing contracts should be excluded from the referenced contract definition and subject solely to Exchange position limits. CME Group also believes this would provide significant clarity to the CFTC, DCMs, and the marketplace with regards to the current and future determination of which futures contracts would fall under the referenced contract definition.

- Question (16) Should the Commission require exchanges to maintain a list of referenced contracts and location basis contracts listed on their platforms?

  Answer: From a practical standpoint, CME Group does not believe the Commission needs to require exchanges to maintain a list of referenced contracts and location basis contracts on their platforms. At the same time, we support coordinating with the Commission to ensure consistency and would commit to publishing this information on our website, likely in the position limit rulebook tables of Chapter 5.

- Question (23) The Commission understands that it may be possible for a market participant trading options to start a trading day below the delta-adjusted federal speculative position limit for that option, but end up above such limit as the option becomes in-the-money during the spot month. Should the Commission allow for a one-day grace period with respect to federal position limits for market participants who have exercised options that were out-of-the money on the previous trading day but that become in-the money during the trading day in the spot month?

  Answer: CME Group supports the wording in the proposed definition of "futures-equivalent" in relation to options, which would use the previous day's delta or the current day's delta to calculate an options futures-equivalent position. In the same definition, we also support allowing one business day to liquidate positions in excess of a limit as a result of an option assignment. With regards to the CFTC's question, CME Group believes if a position including options was below the position limit on a futures-equivalent basis based on the previous day's delta but due to a price move becomes in-the-money and thus over the position limit on a future-equivalent basis at that current day's delta, that participant should be allowed the one-day grace period to get below the position limit. CME Group also believes based on the same logic that if a participant exercises an in-the-money option that results in a position over the position limit, that position would be treated as a position limit violation if the futures-equivalent position was over the position limit based on both the previous day's delta and current day's delta. Unlike a short option holder which is assigned an option, a market participant which exercises an option is in control and has definitive knowledge of what their position is and if the exercising will put them above a position limit. These recommendations are consistent with current CME Group rules.

- Question (34) The Commission has proposed that exchanges submit monthly reports under § 150.5(a)(4). Do exchanges prefer that the Commission specify a particular day each month as a deadline for submitting such monthly reports or do exchanges prefer to have discretion in determining which day to submit such reports?

  Answer: CME Group prefers that the Commission not specify a particular day each month as a deadline for submitting a monthly report under § 150.5(a)(4). We prefer to continue the current process of working with the CFTC to provide the report at the beginning of the month but allowing for flexibility based on schedules. Additionally, writing a deadline into the rule may limit advancements in the process as it may become more automated over time.

- Question (35) Considering that the Commission's proposed position limits would apply to OTC economically equivalent swaps, should the Commission develop a mechanism for

exchanges to be involved in the review of non-enumerated bona fide hedge applications for OTC economically equivalent swaps?

Question (36) If so, what, if any, role should exchanges play in the review of non-enumerated bona fide hedge applications for OTC economically equivalent swaps?

Answer: CME Group is open to reviewing non-enumerated bona fide hedge applications for OTC economically equivalent swaps. However, monitoring of positions and compliance with the rules would have to be done at the CFTC level. CME Group does not obtain complete OTC swap data and surveillance of this activity would have to be done at the CFTC.