

Commodity Futures Trading Commission Proposes Modifications to Regulations on Aggregation With Respect to Position Limits for Futures and Swaps

Overview

On May 30, 2012, the Commodity Futures Trading Commission (the “CFTC”) published a notice of proposed rulemaking (the “Proposed Rules”) modifying the position aggregation provisions in final rules released October 26, 2011 (the “Existing Rules”). The Existing Rules established CFTC-administered speculative position limits for 28 physical delivery commodity futures and options contracts, as well as for swaps that are economically equivalent to such contracts, and largely retained the existing aggregation standards with some modifications. See our [Alert](#) on the Existing Rules. The Proposed Rules would (i) permit any market participant with an ownership interest of from 10% up to 50% in an entity to file for an exemption from aggregation by demonstrating independence in decision making, (ii) modify the definition of independent account controller, (iii) modify the exemption from aggregation based on federal law restrictions and extend the exemption to foreign and state law restrictions, and (iv) extend the exemption from aggregation based on underwriting activities. The CFTC is seeking comment on the Proposed Rules through June 29, 2012.

Proposed Exemption from Aggregation Based on Demonstrated Independence

Under the Existing Rules, for purposes of determining whether a market participant has exceeded CFTC-administered position limits, a market participant generally is required to aggregate positions in accounts in which such market participant, directly or indirectly, has an ownership interest of 10% or more.¹ The Proposed Rules would permit any market participant with an ownership interest of 10% up to 50% in a separately organized entity (an “owned entity”) to make a notice filing of exemption from aggregation by demonstrating independence in decision making. The owned entity could be a financial or a nonfinancial entity that has passive ownership interests.

Under the Proposed Rules, an exemption from aggregation of positions in an owned entity would be available if the following criteria are met:

- The market participant owns less than a 50% ownership interest in the owned entity.
- The market participant and the owned entity do not have knowledge of trading decisions of the other. (Knowledge of overall end-of-day position information will not necessarily constitute knowledge of trading decisions, so long as the position information cannot be used to dictate or infer trading strategies; however, the ability to monitor real-time trading could constitute knowledge of trading decisions.)
- The market participant and the owned entity trade pursuant to separately developed and independent trading systems.
- The market participant and the owned entity have and enforce written procedures to preclude one entity from having knowledge of, gaining access to, or receiving data about, the trades of the other.

¹ Exceptions to the 10% threshold apply for pools or accounts using identical trading strategies, and for investors in pools operated pursuant to CFTC Rule 4.13.

Such procedures must include document routing and other procedures or security arrangements, including separate physical locations, which would maintain the independence of their activities.

- The market participant and the owned entity do not share employees that control trading decisions.
- The market participant and the owned entity do not have risk management systems that permit the sharing of trades or trading strategies with the other.

A notice filing would be required under the Proposed Rule to claim this exemption from the aggregation requirements. The notice must describe how the criteria set forth above are met, and must include a certification by a senior officer with knowledge of the contents of the notice. The notice would be effective upon submission to the CFTC; however, the CFTC subsequently could call for additional information as well as reject, modify, or otherwise condition the exemption. The notice filing would be required to be amended in the event of a material change to the circumstances described therein.

The Proposed Rules provide that higher-tier entities may rely upon an exemption notice filing by an owned entity with respect to accounts or positions specifically identified in the notice.

Proposed Modification to Definition of Independent Account Controller

The Existing Rules provide an exemption from aggregation for customer accounts managed and controlled by independent account controllers, which, with respect to a commodity pool operator exempt under CFTC Rule 4.13, only extends to a general partner. The Proposed Rules would modify this definition to include the managing member of a limited liability company.

Proposed Exemption from Aggregation Based on Restrictions in Foreign and State Laws

The Existing Rules provide an exemption from aggregation where the sharing of information between persons would cause either person to violate federal law and require market participants to file an opinion of counsel specifically identifying the restriction of law and facts particular to the market participant claiming the exemption. The Proposed Rules expand this exemption to laws of foreign jurisdictions and state laws and clarify that the scope of the exemption includes a reasonable risk of a violation from any such law. In addition, the Proposed Rules specifically invite comment on whether the exemption should be expanded to “international” law and “local” law.

Proposed Exemption from Aggregation Based on Underwriting Activities

The Existing Rules provide an exemption from aggregation where an ownership interest is in an unsold allotment of securities. The Proposed Rules would expand the exemption to include situations where securities are owned in anticipation of demand as a part of normal market-making activity, or as a result of a routine life cycle event, such as a stock distribution. However, such proposed exemption would not apply to a broker-dealer who acquires more than a 50% ownership interest in another entity.

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Please contact [Deborah Monson](#) or the Ropes & Gray attorney who usually advises you with any questions you may have or if you would like additional information.