



## U.S. COMMODITY FUTURES TRADING COMMISSION

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### Division of Market Oversight

CFTC Letter No. 16-74  
No-Action  
October 7, 2016  
Division of Market Oversight

#### **Re: Extension of No-Action Relief for Swap Execution Facilities from Certain “Block Trade” Requirements in Commission Regulation 43.2**

Ladies and Gentlemen:

On September 19, 2014, the Division of Market Oversight (“Division”) of the Commodity Futures Trading Commission (the “Commission” or “CFTC”) issued CFTC Letter 14-118 (“No-Action Letter 14-118”) to provide relief for swap execution facilities (“SEFs”) from the requirement in § 43.2 that a swap block trade must “[o]ccur[ ] away from the registered [SEF’s]... trading system or platform.”<sup>1</sup> The no-action letter provided that the Division would not recommend enforcement action against a SEF that has rules and/or procedures that provide for the use of a SEF trading system or platform to facilitate the execution of block trades for swaps that are intended to be cleared,<sup>2</sup> and thus is not complying with § 43.2, provided that certain conditions set forth in the letter were met. On November 2, 2015, the Division issued CFTC Letter 15-60 (“No-Action Letter 15-60”) to extend the relief provided in No-Action Letter 14-118.<sup>3</sup> Absent further action from the Division, No-Action Letter 15-60 will expire on November 15, 2016. By letter dated September 21, 2016, the Wholesale Markets Brokers’ Association, Americas (“WMBAA”)<sup>4</sup> has requested that the Division extend the relief granted in No-Action Letter 15-60 until November 15, 2017 to allow, among other things, more time for the development of a permanent solution.<sup>5</sup>

#### **Background**

Commission Regulation 43.2 defines a “block trade” as, among other things, a publicly reportable swap transaction that “[o]ccurs away from the registered [SEF’s]... trading system or platform and is executed pursuant to the registered [SEF’s]... rules and procedures” (hereinafter the “occurs away” requirement”). In a subsequent rulemaking establishing appropriate minimum sizes for block trades, the Commission further clarified this language by stating that “[by] definition, a

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<sup>1</sup> See CFTC Letter 14-118.

<sup>2</sup> Swaps that are intended to be cleared are swaps (i) of a type accepted for clearing by a derivatives clearing organization (“DCO”), and (ii) intended to be submitted for clearing contemporaneously with execution.

<sup>3</sup> See CFTC Letter 15-60.

<sup>4</sup> The WMBAA is an independent industry body that represents BGC Derivatives Markets, L.P.; GFI Swaps Exchange LLC; tpSEF, Inc.; and Tradition SEF, Inc. Each of these WMBAA member firms is registered with the Commission as a SEF.

<sup>5</sup> Letter from Wholesale Markets Brokers’ Association Americas, Request for Extension of No-Action Relief Letter 15-60 from Commission Regulations 37.9(a)(2) and 43.2 (Sept. 21, 2016) (hereinafter “WMBAA Letter”).

block trade must occur away from the SEF[’s] trading system or platform” and that “[a]ny swap that is executed on a SEF[’s]... trading system or platform, regardless of whether it is for a size at or above the appropriate minimum block size for such swap, is not a block trade under this definition....”<sup>6</sup>

WMBAA references its previous no-action requests, where it informed the Division that the “occurs away” requirement under § 43.2 creates difficulties for SEFs to comply with §§ 1.73<sup>7</sup> and 37.702(b)<sup>8</sup> when performing pre-execution credit screening for block trades for swaps that are intended to be cleared.<sup>9</sup> WMBAA again notes that registered future commission merchants (“FCMs”) are required by § 1.73 to impose risk management requirements and enforce compliance with risk-based limits for proprietary and customer accounts. Further, WMBAA stated that FCMs must use automated means to screen orders for automatic execution on a SEF, but are challenged in their ability to conduct pre-execution credit checks for block trades conducted off-facility. WMBAA has also noted, however, that SEFs are positioned to ensure that FCMs have timely, accurate information needed to facilitate pre-execution credit checks.<sup>10</sup>

In its current letter, WMBAA also states that market participants continue to grapple with the uncertainties caused by the definition and treatment of a block trade under the Commission’s regulations. Accordingly, WMBAA proposes that market participants should be provided with a permanent solution. As an interim measure, however, WMBAA believes that “an extension of the relief granted under [No-Action Letters] 14-118 and 15-60 would allow the WMBAA member firms, other SEFs, market participants, and the Commission time to consider and develop best practices and a permanent solution to the issues attendant to block trades, including amendments to the Commission’s regulations.” Therefore, WMBAA requests the Division to provide an extension of the no-action relief in No-Action Letter 15-60 until November 15, 2017.<sup>11</sup>

## **No-Action Relief**

The Division agrees that SEFs can facilitate the pre-trade credit checks that are required for FCMs and SEFs to comply with §§ 1.73 and 37.702(b), respectively. Therefore, the Division has determined to extend the no-action relief currently provided in No-Action Letter 15-60. During this extended period of relief, Division staff will continue to evaluate best practices and a more

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<sup>6</sup> See Procedures To Establish Appropriate Minimum Block Sizes for Large Notional Off-Facility Swaps and Block Trades, 78 Fed. Reg. 32866, 32904 n.425 (May 31, 2013).

<sup>7</sup> Commission regulation 1.73 requires an FCM that is a clearing member (“Clearing FCM”) of a registered DCO to establish risk-based limits and to screen orders for compliance with those limits. Staff guidance has specified that this requirement applies to orders for execution on or subject to the rules of a SEF, regardless of the method of execution. See Staff Guidance on Swaps Straight Through Processing at 2 (Sept. 26, 2013) (“STP Guidance”).

<sup>8</sup> With respect to orders for execution on a SEF, Commission regulation 37.702(b) requires a SEF to coordinate with each DCO to which it submits transactions for clearing and have rules and procedures to facilitate prompt and efficient processing by DCOs in accordance with Commission regulation 39.12(b)(7). Accordingly, staff guidance further specifies, among other things, that a SEF must facilitate pre-execution screening by each Clearing FCM on an order-by-order basis. See STP Guidance.

<sup>9</sup> See CFTC Letter 14-118 and CFTC Letter 15-60.

<sup>10</sup> The Division has understood that an FCM, which has no involvement in a block transaction occurring away from a SEF’s trading system or platform, would be unable to implement a credit screening of the trade prior to the counterparties’ execution of the block. See CFTC Letter 15-60 at 2. The Division confirms that this no-action relief, similar to No-Action Letter 14-118 and No-Action Letter 15-60, does not affect the compliance requirements for pre-trade credit checks and, as such, does not extend relief from the obligation to obtain a pre-trade credit for block transactions which occur away from the trading system or platform.

<sup>11</sup> *Id.*

permanent solution to the issues involved in screening block trade orders for compliance with risk-based limits including, if appropriate, amendments to Commission regulations.

The Division will not recommend that the Commission take enforcement action against any SEF which has rules and/or procedures that provide for the use of a SEF trading system or platform to facilitate the execution of block trades for swaps that are intended to be cleared and thus not complying with the “occurs away” requirement under § 43.2 during the extended period of relief, provided that the conditions set forth in No-Action Letter 15-60 continue to be met. These conditions are as follows:

- the block trade is not executed on the SEF’s Order Book functionality, as defined in § 37.3(a)(3);<sup>12</sup> the SEF adopts rules pertaining to cleared block trades that indicate that the SEF relies on the relief provided in this no-action letter<sup>13</sup> and requires each cleared block trade execution on a non-Order Book trading system or platform to comply with the requirements set forth in the block trade definition in § 43.2. Specifically, the block trade must:
  1. involve a swap that is listed on a registered SEF;
  2. be executed pursuant to the SEF’s rules and procedures;
  3. meet the notional or principal amount at or above the appropriate minimum block size applicable to the swap; and
  4. be reported to a swap data repository pursuant to the SEF’s rules and procedures and the Commission’s rules and regulations.
- the FCM completes the pre-execution credit check pursuant to § 1.73 at the time the order for a block trade enters the SEF’s non-Order Book trading system or platform;<sup>14</sup> and
- the block trade is subject to void *ab initio* requirements where the swap is rejected on the basis of credit.<sup>15</sup>

This no-action relief shall commence on the date of issuance of this letter and shall expire the earlier of 11:59 pm, Eastern Standard Time, on November 15, 2017, or the effective date of any Commission action with respect to the issues discussed above.

## Conclusion

Market participants should be aware that the no-action position taken herein does not excuse affected persons from compliance with any other applicable requirements of the Commodity Exchange Act or the Commission’s regulations thereunder, in particular, the applicable swap data reporting requirements, clearing requirements, pre-execution credit check requirements, and

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<sup>12</sup> The Division notes that while block trades may not be facilitated through a SEF’s Order Book functionality, pursuant to this no-action relief, SEFs are permitted to use request-for-quote (“RFQ”) functionalities to facilitate the execution of a block trade. The Division notes also that a block trade executed through a SEF’s RFQ functionality pursuant to this no-action relief would not be subject to the minimum participant requirement set forth in § 37.9(a)(3). Finally, the Division notes that trades above the minimum block size may occur on the SEF’s Order Book; however, they will not receive treatment as block trades and will not be afforded a reporting time delay.

<sup>13</sup> These rules should include a citation to this no-action letter as “NAL 16-74, expiring November 15, 2017.”

<sup>14</sup> Consistent with the STP Guidance, the § 1.73 credit check must be done before execution, no matter the means of execution.

<sup>15</sup> See STP Guidance at 5.

straight-through processing requirements.<sup>16</sup> This letter, and the no-action position taken herein, represent the views of the Division only, and do not represent the position or views of the Commission or of any other division or office of the Commission's staff. As with all no-action letters, the Division retains the authority to condition further, modify, suspend, terminate or otherwise restrict the terms of the no-action relief provided herein, in its discretion.

If you have any questions concerning this correspondence, please contact Nancy Markowitz, Deputy Director, Division of Market Oversight, at (202) 418-5453 or [nmarkowitz@cftc.gov](mailto:nmarkowitz@cftc.gov), or Roger Smith, Special Counsel, Division of Market Oversight, at (202) 418-5344 or [rsmith@cftc.gov](mailto:rsmith@cftc.gov).

Sincerely,

Vincent A. McGonagle  
Director  
Division of Market Oversight

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<sup>16</sup> The applicable swap data reporting requirements are set forth under parts 43, 45, and 50 of the Commission's regulations. The applicable clearing requirements are set forth under Commodity Exchange Act section 2(h)(1) and part 50 of the Commission's regulations. The applicable pre-execution credit check requirements are set forth under § 1.73 of the Commission's regulations. The applicable straight-through processing requirements are set forth under § 1.74, § 37.702(b), and § 39.12(b)(7) of the Commission's regulations.