

The Commodity Futures Trading Commission has been formulating proposals based on the Dodd-Frank Wall Street Reform and Consumer Protection Act. The following is a summary of the aspects of those proposals related to trading. Specifically, we have reviewed the rulings related to:

1. Approved trading venues, and
2. Eligible Swaps Transactions (swaps required to be traded through approved venues)

### Glossary for OTC Derivatives

- CEA – Commodities Exchange Act
- CFTC – Commodity Futures Trading Commission
- DCM – Designated Contract Market (exchange model)
- DCO – Derivative Clearing Organization
- “Dodd-Frank” – Wall Street Reform and Consumer Protection Act
- MSP – Major Swap Participant
- Order Book - IDB trading model
- RFQ – Request-for-Quote (CanDeal model)
- SD – Swaps Dealer
- SDR – Swap Data Repository
- SEF – Swap Execution Facility

### 1. SWAP trading venues:

The Commission proposes to implement the execution requirement that all Eligible Swap Transactions must occur on a Swap Execution Facility (SEF) or a Designated Contract Market (DCM), except where no SEF or DCM makes the swap available for trading.

#### SEF Definition and Registration Requirements

The Commission proposes to implement the definition of SEF under CEA Section 1a(50) and the registration requirements under CEA Section 5h by:

- Requiring SEFs to provide a basic functionality that gives all market participants the option to post both firm and indicative quotes to multiple parties, including all other parties participating in the SEF; and
- Providing that SEFs have the option to deploy any trading system or platform that provides the basic functionality noted above, including Request for Quote Systems or Order Books.

#### Request for Quote Systems include:

- Trading systems or platforms in which a market participant must transmit a request for a quote to buy or sell a specific instrument to no less than five market participants in the trading system or platform, to which all such market participants may respond. Any bids or offers resting on the trading system or platform pertaining to the same instrument must be taken into account and communicated to the requester along with the responsive quotes;
- Trading systems or platforms in which multiple market participants can both:
  - » View real-time electronic streaming quotes, both firm and indicative, from multiple potential - counterparties on a centralized electronic screen; and

### 1. SWAP trading venues con't:

- » Have the option to complete a transaction by:
  - Accepting a firm streaming quote; or
  - Transmitting a request for quote to no less than five market participants, based upon an indicative streaming quote, taking into account any resting bids or offers that have been communicated to the requester along with any responsive quotes.
- Any such other trading system or platform as may be determined by the Commission.

#### Order Books include:

- Electronic trading facilities as defined under the CEA;
- Trading facilities as defined under the CEA;
- Trading systems or platforms in which all market participants in the trading system or platform can enter multiple bids and offers, observe bids and offers entered by other market participants, and choose to transact on such bids and offers; and
- Any such other trading system or platform as may be determined by the Commission.

#### **DCM Definition**

Designated Contract Markets (DCMs) are boards of trade (or exchanges) that operate under the regulatory oversight of the CFTC, pursuant to Section 5 of the Commodity Exchange Act (CEA), [7 USC 7](#). DCMs are most like traditional futures exchanges, which may allow access to their facilities by all types of traders, including retail customers.

### 2. Eligible Swap Transaction:

An Eligible Swap Transactions is one which:

- Is subject to the clearing and execution requirements under the CEA;
- Is made available for trading; and
- Is not a block trade.

#### **Submission of Swaps to the Commission for Review**

The Dodd-Frank Act requires a Derivatives Clearing Organization (DCO) that plans to accept swaps for clearing to submit the swaps to the Commission for a determination as to whether the swaps are required to be cleared. The proposed rule sets out the process for DCOs to follow when submitting swaps to the Commission.

The DCO would have to provide a statement that would assist the Commission in the assessment of five specific factors that the Dodd-Frank Act requires the Commission to take into account when reviewing a swap submission:

- The existence of significant outstanding notional exposures, trading liquidity, and adequate pricing data;
- The availability of rule framework, capacity, operational expertise and resources, and credit support infrastructure to clear the contract on terms that are consistent with the material terms and trading conventions on which the contract is then traded;
- The effect on the mitigation of systemic risk, taking into account the size of the market for such contract and the resources of the DCO available to clear the contract;

### 2. Eligible Swap Transaction con't:

- The effect on competition, including appropriate fees and charges applied to clearing; and
- The existence of reasonable legal certainty in the event of the insolvency of the relevant DCO or one or more of its clearing members with regard to the treatment of customer and swap counterparty positions, funds, and property.

#### Commission-initiated Reviews of Swaps

The Dodd-Frank Act requires the Commission on an ongoing basis to review swaps that have not been accepted for clearing by a DCO to make a determination as to whether the swaps should be required to be cleared. If no DCO has accepted for clearing swaps that the Commission finds would otherwise be subject to a clearing requirement, the Commission would investigate the relevant facts and circumstances and, within 30 days of the completion of its investigation, issue a public report containing the results of the investigation. The Commission would take such actions as it determines to be necessary and in the public interest, which may include establishing margin or capital requirements for parties to the swaps.

#### Appropriate Minimum Block Size

The proposed rules specify a procedure using two tests – the distribution test and the social size test – to determine the appropriate minimum block size for a block trade and large notional transaction.

The distribution test determines the transaction size that is larger than 95 percent of transactions for that category of swap instrument over the past calendar year.

The social size multiple test is the transaction size that is five times the largest of the mean, median, and mode of transaction sizes for that category swap instrument over the past calendar year.

The appropriate minimum block size would be the larger size determined by those two tests. SDRs would be responsible for determining the appropriate minimum block size.