Via Electronic Mail

May 28, 2014

Ms. Melissa Jurgens
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: OneChicago, LLC Security Futures Product Rule Submission
Block Trade Minimum Threshold – Notice to Members 2014-6
(OCX Submission #14-003)

Dear Ms. Jurgens:

Pursuant to section 5c(c)(1) of the Commodity Exchange Act, as amended (the "Act"), and § 40.6(a) and § 41.24 of the regulations promulgated by the Commodity Futures Trading Commission ("CFTC" or the "Commission") under the Act, OneChicago, LLC ("OneChicago," "OCX," or the "Exchange") hereby submits the following rule change and corresponding Notice to Members ("NTM"), which will become effective on June 12, 2014. The amendment will make the following change to OCX's block trading program: OCX Rule 417 will be modified to decrease the minimum block trading quantity from twenty-five contracts to five contracts for its OCX.NoDivRisk® ("NoDivRisk") products.

Currently, OCX Rule 417 sets the minimum block trade threshold at twenty-five contracts. That quantity was the result of a pilot program enacted by the Exchange in September 2012. OCX is now proposing to reduce its minimum block trade threshold to five contracts for block trades in its NoDivRisk contracts. OCX is decreasing its minimum block trade threshold in these contracts for two reasons: First, because products substantially similar to OCX's innovative NoDivRisk futures are expected to be introduced on foreign exchanges for U.S.-listed equities with no minimum block size thresholds, posing a serious competitive disadvantage for the Exchange. Secondly, this reduction is appropriate because the majority of NoDivRisk block trades are financing trades, and not long/short risk position trades that play a role in price discovery.

Alternative Single Stock Futures Execution Venues

At least one foreign exchange, through its block trade reporting facility, now offers, or may soon offer, single stock futures ("SSFs") on U.S.-listed equity underlyings substantially similar to OCX.NoDivRisk products.[1] This venue permits privately-negotiated trades with no minimum threshold. Accordingly, disparate privately-negotiated trading regimes will lead to regulatory arbitrage, as market participants rush to the jurisdiction where regulation permits the lowest cost of trading with the least operational friction.

The foreign exchange has recently introduced dividend adjusted SSFs, which mirror OCX's innovative product—the OCX.NoDivRisk. OCX.NoDivRisk futures adjust for dividends on the morning of ex-dividend date in order to remove dividend variation risk. On the basis of discussions with our current customers, OneChicago has come to believe that without comparable block minimum thresholds, there is a high probability that SSF trading on U.S. equities will migrate from the United States to foreign jurisdictions.

The OCX.NoDivRisk product, a OneChicago innovation, was introduced in 2010 and has been well-received by the marketplace, representing more than half of total open interest and all of OneChicago's Commodity Trading Advisor ("CTA") business. Additionally, the NoDivRisk product helped join the futures industry (CTA customers) and the securities industry (liquidity providers), as both industries benefit from participation in the SSF market, albeit for different reasons. The dividend adjusted futures that are now offered by a foreign exchange replicate OCX's products, and trading in this innovative, U.S.-based product is now threatened by imitation in other jurisdictions. With the introduction of these products and the less restrictive regulatory environment in Europe, the foreign exchange is poised to take over not only many of OCX's customers, but also the liquidity providers to those customers. In effect, OCX's NoDivRisk SSF trading may soon entirely shift to a foreign jurisdiction solely due to regulatory arbitrage.

Congressional Intent

In 2000, Congress passed the Commodity Futures Modernization Act ("CFMA"), which allowed for the trading of SSFs in the United States. When passing the CFMA, Congress' well-documented intent was to level the playing field with regard to SSF trading in the U.S., which had been previously prohibited in the U.S. by the Shad-Johnson Accord, but was permissible in foreign jurisdictions.[2] OCX's proposed rule amendments directly support Congressional intent

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[1] The foreign exchange currently offers SSFs on U.S.-listed equities, but does not yet offer dividend-adjusted SSFs on U.S.-listed equities. OCX has been made aware by a customer that the foreign exchange intends to list dividend-adjusted SSFs on U.S.-listed equities in the near future.

[2] "The threat to U.S. markets has increased in just the last month. The London International Financial Futures Exchange [LIFFE] announced that it would begin trading single stock futures on U.S. based company stocks in January 2001. In just three months, futures on the stock of AT&T, Citigroup, Cisco, Systems, Exxon Mobil, and Merck will be traded in London. If H.R. 4541 [the Commodity Futures Modernization Act] does not pass, U.S. markets will continue to be prohibited from offering these products-handcuffed from competing with foreign exchanges for a U.S. market that should be traded here at home. Let me be clear, this is not just an Illinois issue. Futures exchanges are a huge part of what makes the entire U.S. economy robust and vibrant. If we fail to lift the ban on single stock futures, if we fail to provide regulatory reform, and if we fail to provide legal certainty to U.S.

in enacting the CFMA, as the effect of the rule change described herein is to facilitate the trading of SSFs on U.S.-listed equities on U.S. venues in a manner comparable to foreign SSF execution venues.

OCX Block Trading – Single Stock Futures Financing

Major market participants utilize NoDivRisk block trades to access financing provided by a liquidity provider in large notional value transactions. These liquidity providers do not act as market-makers in the traditional sense of readiness to take on market risk to produce a two-sided market. Rather, these particular liquidity providers stand ready to offer synthetic delta risk exposure for a return on their capital. These types of transactions do not involve two distinct risk positions. The party seeking the risk position (the customer) wants synthetic delta exposure to the underlying equity. "Delta One Desks" at major banks (the liquidity providers) are willing to provide that synthetic exposure by extending their balance sheet in a riskless transaction that generates yield.[3]

Liquidity providers utilize their balance sheets by hedging their sales/purchases of SSFs to customers with purchases/sales in the underlying equity. Essentially, the liquidity provider gives the customer the desired delta exposure without being exposed to directional market risk itself. The liquidity provider's only intent is to buy/sell the two equivalent positions at a price differential—as the futures contract expires, the position flattens out and the long stock position is used to satisfy the short futures obligation, or vice versa. The liquidity provider's gain is captured as the difference between the price at which it sold stock/bought futures or sold futures/bought stock. Critically, the liquidity provider must purchase/sell an equivalent number of underlying shares in order to price the SSF correctly.

For example, a customer instructs a liquidity provider that the customer would like synthetic long exposure to 50,000 shares of ABC Co. at a limit price up to $20.00/share with an agreement to price the synthetic (SSF) forty basis points higher than the Volume Weighted Average Price ("VWAP")[4] of the liquidity provider's hedge for the desired term. The liquidity provider then begins to execute its 50,000 share hedge in the equity underlying at prices up to the limit price of $20.00/share. The liquidity provider returns to the customer with a VWAP based on its hedge in the underlying, and then "tacks on" the agreed upon basis to arrive at the futures price. Therefore, if the liquidity provider was able to complete the hedge at a VWAP of $19.87 for example, it would then "tack on" the agreed upon forty basis points. In this case, the cost of the

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derivatives markets, then the consequences could be devastating. For example, U.S. exchanges will be rendered completely unable to compete. Without this legislation, single stock futures, *which are based on assets developed and produced in the United States*, may never be traded in this country." 146 CONG. REC. H10416 (Oct.19, 2000) (statement of Rep. Davis on the Commodity Futures Modernization Act of 2000) (emphasis added). OCX agrees with Representative Davis' statement regarding SSF trading in the U.S and finds his comments particularly relevant to this discussion. U.S. SSF trading is currently threatened by foreign markets emulating the success of the OCX.NoDivRisk contract, an innovative product that was created in the U.S.

[3] These groups are often referred to as "Delta One Desks" because they deal in derivatives that may serve as "delta one" synthetic equivalents of their underlying equities. These derivatives include equity options, equity swaps, and single stock futures.

[4] VWAP is a method of trading in which the price of the completed trade is the average price of each trade, weighted by the volume of shares at each price level inside a time range.

futures would be $19.8738, which reflects the interest for the term added to the VWAP price of $19.87. The interest is calculated using three variables: the stock price ($19.87), the term (in this case, assume the parties trade on April 4 and trade in the April expiry futures that expire on April 21, which results in a 17 day term), and the basis points (40 basis points, or the equivalent of 0.40%, which when expressed as a numerical decimal is .004). Therefore, $19.87 × (.004/360) × 17 = $0.003753. This figure represents the per share cost of holding the equity position. To calculate the customer's total cost (and therefore the total profit for the liquidity provider) for the 17 day term, that amount is multiplied by the number of shares: $0.00375 × 50,000 = $187.65.

The liquidity provider is able to generate yield on its cash without taking on directional market risk. The customer, on the other hand, is able to acquire synthetic delta exposure to the underlying stock (at the cost of the interest rate). By removing dividend risk, the OCX.NoDivRisk contract allows the above trade to be a pure financing transaction. The NoDivRisk contract adjusts for all distributions on the ex-dividend date. Without this feature, SSF participants run the risk that actual distributions may differ from expected distributions, leading to an unanticipated (and undesirable) directional loss or gain.

Since the above trade is a financing trade, any additional fee or operational friction that is introduced to the transaction reduces the efficiency of the trade. Regulatory imbalances with regard to block trade thresholds provide the incentive to migrate volume to the jurisdiction with the least regulatory and operational friction. It would be difficult to recapture lost order flow once volume is lost. Accordingly, OCX is making this rule amendment proactively in an attempt to prevent such a loss of order flow, which would potentially be catastrophic for the Exchange and SSF trading in the U.S.

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The purpose and effect of the rule change is to permit market participants to trade bilateral blocks with a minimum threshold of five contracts. Comments on this NTM have not been solicited and none have been received. OneChicago is not aware of any substantive opposing views to this NTM. OneChicago certifies that the NTM complies with the Act, including the core principles, and the Commission's regulations promulgated thereunder. OneChicago further certifies that a copy of this submission has been posted on the OneChicago website. OneChicago staff has reviewed the core principles applicable to designated contract markets ("DCMs"), and has concluded that the proposed NTM may have some bearing upon the following core principles:

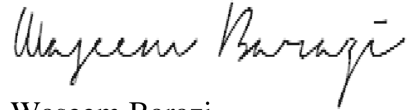
Core Principle 7: Core Principle 7 requires that a DCM make available to market authorities, market participants, and the public accurate information concerning the rules, regulations and mechanisms for executing transactions on or through the facilities of the contract market. This NTM supports Core Principle 7 in that it informs market participants of the manner in which block trades can be reported to the Exchange.

Core Principle 9: Core Principle 9 allows a DCM to authorize market participants to enter into or confirm the execution of a contract for the purchase or sale of a commodity for future delivery if the contract is traded in accordance with the rules of the contract market. The block trade

minimum threshold permitted by this rule change is designed to permit market participants to execute these transactions in accordance with Exchange Rules, and in accordance with market practice in other SSF execution venues.

If you have any questions or comments related to this filing, please feel free to contact me by telephone at (312) 424-8524 or through e-mail at wbarazi@onechicago.com.

Respectfully Submitted,



Waseem Barazi
Chief Regulatory Officer

Encl: Attachment A
Attachment B

<u>**Attachment A**</u>

417. Block Trading

(a) Clearing Members, Exchange Members and Access Persons may enter into transactions at reasonable prices mutually agreed, with respect to Contracts that have been designated by the Exchange for such purpose, provided all of the following conditions are satisfied (such transactions, “Block Trades”):*

(i) Each buy or sell order underlying a Block Trade must (A) state explicitly that it is to be, or may be, executed by means of a Block Trade and (B) be for at least <u>5 Contracts in the OCX.NoDivRisk futures and at least </u>25 Contracts<u> for all other products</u>; *provided* that only (x) a commodity trading advisor registered under the CEA, (y) an investment adviser registered as such with the Securities and Exchange Commission that is exempt from regulation under the CEA and Commission Regulations thereunder and (z) any Person authorized to perform functions similar or equivalent to those of a commodity trading advisor in any jurisdiction outside the United States of America in which the Exchange may be permitted from time to time to operate OneChicago Workstations, in each case with total assets under management exceeding US$25 million, may satisfy this requirement by aggregating orders for different accounts.

(a)(ii)-(h) – No Change

Attachment B

Notice to Members 2014-6

Date: May 28, 2014

Re: OCX.NoDivRisk Block Trade Minimum Threshold

Effective Date: June 12, 2014

OneChicago, LLC ("OCX") is modifying its block trading Rule to decrease its minimum block trading quantity from twenty-five to five contracts for its OCX.NoDivRisk® products.

Five Contract Block Trade Minimum

OCX has amended its Rulebook to provide for a minimum block size of five contracts for its OCX.NoDivRisk products. Accordingly, this Notice to Members ("NTM") supersedes NTM 2012-25 solely with regard to the block trade minimum quantity threshold. The OCX.Original ("1C") product will remain at a block trade minimum quantity threshold of twenty-five.

Any questions can be directed to marketsurveillance@onechicago.com or (312) 424-8530.