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COMMENT
CL-02693

19 April 2010

Mr. David Stawick
Secretary
Commodity Futures Trading Commission
1155 21st Street, NW
Washington, DC 20581

Dear Mr Stawick

Position Limit Rule Consultation

On 26 January 2010 the Commission issued a Notice of proposed rule making outlining proposals with respect to the revision of the existing position limit rules with respect to certain energy contracts[1]. This letter sets out ICE Futures Europe's response to those proposals.

Background

ICE Futures Europe ("the Exchange") is Europe's largest energy futures exchange and the second largest in the world. ICE Futures Europe is the home of the ICE Brent Crude Futures Contract which is the primary benchmark for crude oil pricing outside the United States. ICE estimates that the North Sea Brent Complex of which ICE Brent Futures is a part is used in the pricing of two-thirds of the world's traded oil. The Exchange also operates the ICE Gas Oil Futures contract, which is the international benchmark for refined oil products such as diesel, as well as European and Asian futures contracts in coal, natural gas and power. With its partner, the European Climate Exchange, ICE Futures Europe also operates the world's largest carbon market.

ICE Futures Europe is a UK Recognised Investment Exchange regulated by the UK Financial Services Authority ("FSA") in accordance with the Financial Services and Markets Act 2000. The Exchange is headquartered in London where it was founded in 1981 as the International Petroleum Exchange of London Limited. ICE Futures Europe maintains extensive regulatory, compliance and market supervision staff, all of which are based at its London headquarters. All ICE Futures Europe Contracts are cleared by ICE Clear Europe, a Recognised Clearing House, regulated by the FSA. ICE Futures Europe and ICE Clear Europe are subsidiaries of IntercontinentalExchange (NYSE: ICE) a global operator of regulated futures exchanges, OTC marketplaces and clearing facilities,

[1] Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations; Proposed Rule *Federal Register, 26 January 2010*

headquartered in Atlanta, Georgia. The development and operation of ICE Futures Europe's electronic trading platform is outsourced to IntercontinentalExchange.

Since 1999, the Exchange has had permission to operate electronic trading terminals in the United States under the terms of a series of 'No Action' letters issued by the Commission. The CFTC's mutual recognition system is an important component of the cooperation among regulators in an increasingly global marketplace. This cooperation is necessary to ensure a fair, well-regulated and efficient global marketplace.

ICE WTI Futures

In February 2006, the Exchange introduced the ICE WTI Futures contract in response to customer demand for an electronic, transparent WTI. At that time, no other electronic WTI futures contract was offered due to the prevailing open-outcry model in the US, where direct access was limited to those on the trading floor. ICE's electronic WTI Futures grew rapidly in popularity, with traded volumes increasing from some 40,000 contracts per day in February 2006 to 173,000 contracts per day in March 2010. The ICE WTI Futures contract is financially-, or cash, settled against the prevailing WTI price. This is currently the settlement price of the NYMEX physically-delivered light sweet crude oil contract on the day prior to contract expiry.

Since 1999, the Exchange has had permission to operate electronic trading terminals in the United States under the terms of a CFTC 'No Action' letter. The terms of this letter have been updated on a number of occasions, most recently on 20 August 2009[2]. Under the terms of the revised No Action letters, ICE Futures Europe operates under regulation of both its home country regulator, the FSA, as well as under the regulatory requirements of the US Commodity Futures Trading Commission for all "linked contracts". As a result, ICE Futures Europe applies an equivalent regulatory framework for reporting, position limits and position accountability levels to the linked markets that are set by and required in those operated by NYMEX. As such, the cash-settled ICE WTI Futures contract has a position limit of 3,000 contracts in the last three days leading up to contract expiry (subject to applicable bona fide hedge exemptions), and the Exchange also operates position accountability levels. In addition, clearing members are required to report all client positions in excess of 100 contracts on a daily basis to the Exchange's compliance department and this information is shared with the Commission. The Commission uses the aggregate data reported by the Exchange to produce and publish a 'Commitment of Traders' report on a weekly basis for the ICE WTI Futures similar to those produced with respect to Designated Contract Markets.

The No Action letters impose a number of additional regulatory and reporting obligations on ICE Futures Europe including *inter alia*, the provision of daily trade data, the notification of all rule

[2] CFTC Letter 09-37 http://cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/09-37.pdf

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amendments and disciplinary actions with respect to linked contracts, and cooperation with the CFTC in the event that Emergency Action is directed pursuant to the Commodity Exchange Act Section 8a(9).

The Commission's Proposals

The Commission's proposed rulemaking relates to four energy contracts, all of which have underlying delivery points based within the United States, and the rules will apply principally to US exchanges and over-the-counter (OTC) markets. The determination of the appropriate regulatory regime for such contracts is a matter for American regulators and Congress to determine, just as the appropriate regulatory regime for the determination of the treatment of North Sea Brent Crude oil should be determined by UK regulators and Parliament. This letter will not, therefore, comment on all aspects of the Commission's proposals but will address two areas:

- a comment on ICE Futures Europe's approach to the management of large positions; and
- specific responses to questions 12 and 13 which concern the impact of the proposed rules on Foreign Boards of Trade.

Position management

As outlined above, ICE Futures Europe has cooperated fully with the Commission in implementing the terms of a series of revised No Action letters and intends to continue to do so in combination with working with the FSA to ensure continued compliance in an evolving global market place.

For contracts other than "linked contracts", the Exchange operates a position management regime. Each of these other contracts trades with reference to European, Asian or Middle Eastern delivery points. ICE Futures Europe requires that clearing members report all client positions to the Exchange on a daily basis, subject to a minimum reporting threshold of 100 contracts with respect to oil contracts. The Exchange monitors all such client positions and where positions are substantial will contact the member and client concerned to determine the purpose for which such positions are held. This is most important with respect to physically-delivered contracts where there are limits on delivery capacity, such as ICE Gas Oil Futures. In the case of Gas Oil Futures, during the final month of trading in a contract, the Exchange will contact holders of significant Gas Oil positions to confirm their intent and capability of making or taking delivery and the Exchange may require that positions be reduced to limit position concentration and ensure price convergence. At any point during the month where clients hold positions which it regards as excessive, the Exchange will advise members to reduce such positions.

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The FSA addresses the same issues with respect to market concentration as US regulators. Below is an excerpt from their testimony to Parliament in July 2008:

"We require exchanges to monitor their markets to check what positions are being established across the full life of a contract, on a real-time and ongoing basis. They share these position reports with us and we review them as part of our market monitoring activity. The exchanges' rules give them authority to manage positions at any time throughout a contract life cycle and to instruct a member to close or reduce a position with the exchange, if that is necessary to secure fair and orderly markets. If the member does not comply, the exchange can close the position unilaterally. There is considerable precedent for this action. We believe that in these ways UK arrangements already provide equivalent standards of protection to those in the US."

The principal purpose of this position management regime is to ensure that market manipulation is prevented. The CFTC has obligations with respect to 'excessive speculation' and the Exchange has its own responsibility with respect to the operation of a 'fair and orderly market'. However the Exchange has not seen any evidence as to the existence of excessive speculation, nor has the position limits regime been effective in managing price levels or volatility. Indeed there is a risk that restrictive position limits might reduce the liquidity available in US markets, which could increase price volatility of US contracts, particularly in the run-up to contract expiry. This could be to the detriment of commercial market participants who participate in expiry. The UK Financial Services Authority and UK Treasury in their joint publication 'Reforming OTC Derivative Markets: a UK Perspective'[3] set out their perspective:

"In relation to controlling or limiting price movement, we have seen no evidence to suggest that one particular type of market participant has been solely responsible for systematically driving derivative market prices. As a result, we do not believe that limiting one class of market participant by imposing specific limits is a desirable or warranted response to the changing nature of derivative markets. Furthermore, there is no evidence to date which demonstrates that prices of commodities, or other financial derivatives, can be effectively controlled through the mandatory operation of regulatory tools such as position limits. We therefore do not believe these measures would achieve the goal of solving the perceived problems."

Foreign Boards of Trade

The Commission in its Request for Comment has requested responses to two specific questions which concern Foreign Boards of Trade.

[3] Financial Services Authority & HM Treasury *Reforming OTC Derivative Markets: A UK perspective* http://www.fsa.gov.uk/pubs/other/reform_otc_derivatives.pdf

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12. As discussed previously, the Commission has followed a policy since 2008 of conditioning FBOT no-action relief on the requirement that FBOTs with contracts that link to CFTC-regulated contracts have position limits that are comparable to the position limits applicable to CFTC-regulated contracts. If the Commission adopts the proposed rulemaking, should it continue, or modify in any way, this policy to address FBOT contracts that would be linked to any referenced energy contract as defined by the proposed regulations?

The Exchange has worked closely with the CFTC over the past decade on continuing to evolve the No Action Letter framework and expects to continue to do so. Whatever the Exchange's views on the merit of the Commission's proposals, it is clearly appropriate for Exchanges that offer linked-contracts to operate under the rules that apply to US Exchanges, though this is currently only applied to ICE Futures Europe, despite the existence of 30 Foreign Boards of Trade in the US. Accordingly we propose:

- that for the purpose of the calculation of Aggregate position limits, positions which are held on Foreign Boards of Trade should be included in the calculation of aggregate open interest;
- Foreign Boards of Trade which operate linked contracts would have the terms of their No Action Letters amended to ensure that they agree to cooperate with the implementation of aggregate position limits and (should the Commission choose to proceed with reporting market position limits) to implement reporting market position limits.

In order to implement such limits, ICE Futures Europe may need to make rule changes which would need to be approved by the FSA in accordance with the Investment Exchanges and Clearing Houses Act 2006[4]. We respectfully request that any changes to the ICE Futures Europe No Action Letter resulting from these proposals be made with sufficient notice to allow full consultation with the FSA with respect to the method of implementation. We further note that Futures Commission Merchants will need to make a number of system changes and enhancements in order to allow them properly to monitor aggregate positions across separate exchanges. These changes will require development work by third party vendors; again we respectfully request that the Commission take account of such technology development timelines in determining the notice period for the introduction of any aggregate position limits.

13. The Commission notes that Congress is currently considering legislation that would revise the Commission's section 4a(a) position limit authority to extend beyond positions in reporting market contracts to reach positions in OTC derivative instruments and FBOT contracts. Under some of these revisions, the Commission would be authorized to set limits for positions held in OTC derivative

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[4] The Investment Exchanges and Clearing Houses Act 2006 confers on the Financial Services Authority the Power to disallow excessive regulatory provisions. It was designed to prevent exchange owners based outside the UK from imposing excessive regulation on UK-based exchanges and clearing houses.

instruments and FBOT contracts. The Commission seeks comment on how it should take this pending legislation into account in proposing Federal speculative position limits.

With respect to the setting of limits for positions held in FBOT contracts, the Commission's focus is properly on Linked Contracts as set out in response to Question 12 above. We believe that the establishment of position limits on FBOT linked contracts addresses concerns about the need for equivalent regulatory treatment of linked contracts.

The question arises as to whether it is appropriate for the Commission to oblige a regulated Foreign Board of Trade to apply position limits with respect to non-US contracts, or contracts other than linked contracts. We believe that it would be inappropriate to do so for two primary reasons:

(1) US customers have access to many contract markets in globally traded commodities markets for price discovery where reference pricing is based on delivery points outside the US. For example, the ICE Gas Oil Futures contract is physically delivered in the Amsterdam-Rotterdam-Antwerp region of north-west Europe and is primarily used by European and Asian market participants. We believe that the determination of the appropriate position limit regime for this contract is a matter that ICE Futures Europe should determine within the well established FSA position management framework , subject to UK and EU law. For the Commission to seek to impose position limits on non-US contracts would be extra-territorial, inappropriate and unjustified.

(2) A number of US exchanges listed contracts with delivery and/or pricing points outside the US but not directly regulated by local regulators at the delivery point. For example, the ICE Futures U.S. sugar futures contract has many delivery points around the world. Other US futures exchanges list interest rate contracts based on interest rates determined in the UK. Were the Commission to seek to extend the imposition of position limits to contracts other than linked contracts, for example to contracts with certain delivery points in the US, they might invite retaliatory action against such US exchanges from overseas regulators. This could unintentionally lead to circumstances where global commodity derivatives markets were subject to multiple and, on occasions, conflicting regulation.

The Commission has taken a leading role in promoting cooperation between regulators around the world and we continue to take the view that the development of an appropriate framework for international commodity market issues is best served by further cooperation between regulators through the IOSCO framework.

Conclusion

The No Action framework within which US market participants are allowed direct access to Foreign Boards of Trade has worked well, bringing more choice and price transparency to US customers, as well as competition to US derivatives markets and spurring innovation and enhanced risk management practices in the US ICE Futures Europe recognises the legitimate interest of the Commission in ensuring that contracts linked to US contracts traded on US

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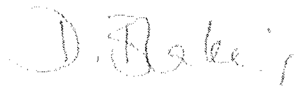
exchanges are appropriately regulated and subject to a consistent regulatory approach. The Exchange looks forward to continuing to work closely with the Commission and the FSA to ensure that international energy futures markets remain effectively and appropriately regulated.

Yours sincerely



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