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IntercontinentalExchange

IntercontinentalExchange, LLC  
2100 RiverEdge Parkway, Suite 400  
Atlanta, GA 30328

August 4, 2000

Ms. Jean A. Webb  
Office of the Secretariat  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1125 21st Street, N.W.  
Washington, D.C. 20581

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OFFICE OF THE SECRETARIAT

Re: New Regulatory Framework for Multilateral  
Transaction Execution Facilities, Intermediaries  
and Clearing Organizations 65 Fed. Reg. 38995 (June 22, 2000)

Dear Ms. Webb:

This is in response to the request for comments on the proposal by the Commodity Futures Trading Commission (the "Commission") to adopt a new Part 37 of the Commission's regulations under the Commodity Exchange Act (the "Act"), providing for an exemption from most provisions of the Act for derivative transaction facilities ("DTFs") and transactions conducted on or through such facilities (the "Proposal"). The comments set forth below are submitted on behalf of IntercontinentalExchange, LLC ("Intercontinental"), a Delaware limited liability company that is in the process of establishing, and will operate, an electronic platform (the "Platform") for the trading of physical commodities and derivative products on such commodities among commercial participants.

As described in greater detail in a written request for no action relief submitted to the Commission on April 7, 2000 (the "No Action Request"), Intercontinental's founding equity owners include the following companies or their affiliates: BP Amoco, Deutsche Bank, Goldman Sachs, Morgan Stanley, Royal Dutch/Shell, Société Générale, Elf Trading, MHC Investment Company and Continental Power Exchange, Inc. In addition, since the date of the No Action Request, the following entities have also indicated their intention to become equity owners: American Electric Power, Aquila Energy, Duke Energy, El Paso Energy, Reliant Energy and Southern Company Energy Marketing. Intercontinental expects that its participants will initially utilize the Platform in order to trade a variety of energy and metals-based products. Among the derivative products to be traded on or through the Platform will be "swap agreements", as defined in Commission Regulation § 35.1 of the Act, as well as options and forward contracts.

The Proposal constitutes a significant step towards alleviating the regulatory burdens and restrictions imposed on derivative markets in the United States. It is innovative in that it recognizes that varying degrees of regulation are appropriate for different types of markets, depending on their participants and other characteristics. Furthermore, at least in principle, the Proposal acknowledges the need for electronic trading platforms to be able to commence operations without a lengthy approval process and to react flexibly and expeditiously to the needs and requests of their participants.

In our view, however, the overall approach reflected in the Proposal is fundamentally inconsistent with the nature of the over-the-counter markets for commodities and derivatives and is inappropriate and unnecessary in the context of DTFs that are accessible solely by commercial participants ("Commercial DTFs"). In particular, the Proposal applies the traditional futures exchange regulatory model to DTFs and then exempts them from specified, limited portions of that regulatory scheme. This approach, we believe, will result in the imposition of excessive and unwarranted burdens on Commercial DTFs and will make it virtually impossible for them to operate. In fact, if the Proposal is adopted in its current form, we believe that Commercial DTFs will seek to operate outside of the Commission's regulatory regime, even if this requires extraordinary measures, such as confining their operations to areas outside of the United States. This will obviously serve only to undermine the achievement of the Commission's stated objectives, to the detriment of the markets, market participants and the public. We therefore strongly recommend that the Commission modify the Proposal in the manner suggested in this letter and the attachment.

For the reasons stated in the No Action Request, Intercontinental believes that the Platform constitutes the type of transaction execution facility for which an exemption from most provisions of the Act is most clearly appropriate.\* Intercontinental, and other similar types of facilities or platforms, seeks to replicate practices in the existing over-the-counter and voice broker markets, in which commercial participants enter into principal-to-principal transactions either through direct communications with each other or through voice brokers. Electronic trading facilities simply represent a more efficient and less costly means of effecting transactions that are currently conducted through these types of direct or indirect telephone communications. The participants in these markets are comprised exclusively of commercial entities that are regularly engaged in businesses related to the underlying physical commodities or over-the-

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\* We note in this connection that, by letter dated May 8, 2000, the Commission granted the relief sought by Intercontinental in its No Action Request. As set forth in the No Action Request, we do not concede that the transactions to be effected through the Platform will constitute futures contracts or that the Platform itself will constitute a "multilateral transaction execution facility" for purposes of Part 35 of the Commission's regulations under the Act or will in any way be subject to the jurisdiction of the Act or the Commission's regulations thereunder.

counter derivative products based on such commodities and generally enter into transactions solely for their own accounts. Accordingly, the participants in these markets are not seeking to replicate, or establish substitutes for, traditional futures exchanges, nor do they require the regulatory protections that are extended to the public participants in such exchanges.

Based on these considerations, and on our analysis of the Proposal and the existing regulatory regime, we have prepared an alternative proposal (the "Alternative Proposal") regarding a regulatory framework for Commercial DTFs. See Attachment I hereto. The Alternative Proposal, in our view, will better serve the interests of the Commission and the markets by creating a stand-alone set of regulations that can be readily understood and applied without reference to other parts of the Act and Commission regulations. Certain significant features of the Alternative Proposal, and the major differences between the Commission's Proposal and the Alternative Proposal, are summarized in the following paragraphs.

- *Streamlined Approval Process.* In our view, it is essential for the viability of the DTF model that it provide for a streamlined procedure pursuant to which qualifying facilities will be recognized by the Commission within a fixed time period. As noted, the business model for Commercial DTFs is not that of traditional futures exchanges; they are based instead on the model of the current voice broker system in the over-the-counter markets, in which business can be commenced quickly and easily. Moreover, because the over-the-counter market consists of commercial entities trading on a principal-to-principal basis, a DTF will typically not have futures exchange-style memberships or rules. Any substantive review of Commercial DTFs, their owners or operators, therefore, or any review of rules or principles applicable to trading on or through such facilities, would be inappropriate and unwarranted and will render the DTF framework completely unworkable. In fact, rather than submit to an exchange-style regulatory system, we believe that Commercial DTFs will take whatever steps are necessary to operate in a manner that does not require qualification as a DTF, even if that means conducting their activities exclusively offshore. This result is clearly contrary to the the interests of the Commission, the markets and the public. In contrast, the recognition procedure set forth in § 37.3 of the Alternative Proposal, avoids the imposition of an unnecessary and impracticable approval process while still ensuring that the Commission will have available to it all documents and information provided to participants of each DTF, as well as certain documents and information relating to corporate matters. The Alternative Proposal is therefore better suited to the nature and objectives of Commercial DTFs but does not compromise the Commission's regulatory interests.
- *Departure from Traditional "Rule" and "Contract" Concepts.* It is important to recognize, as noted above, that electronic trading facilities such as the Platform do not have, and have no need for, "rules" of the type relied upon by traditional

forms of contract markets. Instead, they will develop trading protocols, product descriptions, fee schedules, user guides and similar trading or transaction related documents or information as may be appropriate in light of the relevant markets and their participants. Similarly, exchange-centered notions such as the “listing” of contracts are completely inapplicable to Commercial DTFs, which will simply allow participants to trade the over-the-counter products they wish to trade but will not themselves sponsor or develop “contracts”. In fact, these facilities will likely derive a substantial part of their trading volume from transactions resulting from requests for quotations posted by participants with respect to products they wish to trade. The Alternative Proposal omits any references to “rules”, the “listing of contracts” or any approvals required therefor. Section 37.3(a) and similar provisions have been drafted to reflect the fact that the types of contracts traded and transactions conducted, as well as the number and type of participants, will vary significantly between different Commercial DTFs and over time, and will necessarily result in different arrangements regarding market structure and documentation. Any attempt to confine Commercial DTFs to a particular structure, or to unsuitable traditional exchange concepts, will render the Proposal virtually useless for Commercial DTFs.

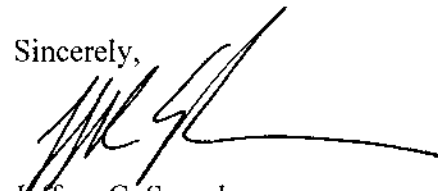
- *Limited Set of Obligations.* We endorse the Commission's proposal to require DTFs to comply with a limited number of core principles to be set forth specifically in part 37 of the Commission's regulations. The advantages of this approach will be completely undermined, however, if DTFs are also subjected to the application of other, general provisions of the Act and the Commission's regulations, many of which can only meaningfully be applied to traditional futures exchanges. Section 37.2(c) of the Alternative Proposal takes into account that references to a limited number of provisions in other parts of the Commission's regulations might be necessary to establish sufficient authority for the Commission to grant the exemptive relief afforded by, and enforce the provisions of, part 37. Any additional cross-references will result in the “importation” of concepts and interpretations from the regulatory scheme applicable to traditional contract markets, and must therefore be avoided. In applying this principle to the Alternative Proposal, we have limited the additional obligations applicable to DTFs to those specifically set forth in § 37.5. We believe strongly that any other extraneous provisions incorporated in the Proposal have no applicability to Commercial DTFs and will serve only to make the exemption unworkable for DTFs, thereby undermining realization of the Commission's stated objectives.
- *No Commission Jurisdiction Over Participants.* It is not appropriate for the Commission to establish jurisdiction over participants on the basis of their trading through Commercial DTFs. Obviously, to the extent that participants are otherwise subject to the Commission's jurisdiction, the Commission's resulting

powers and authority will remain unaffected by the exemption granted under part 37. On the other hand, if the adoption of part 37 results in the Commission expanding its jurisdictional reach over parties to transactions executed through DTFs, it is clear that many participants will refuse to participate in DTFs and will simply continue to conduct their over-the-counter business through traditional means or offshore. This will have a chilling effect on the future development of Commercial DTFs, at least in the United States.

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We appreciate this opportunity to comment on the Proposal. Please feel free to contact the undersigned at any time if you wish to discuss the Alternative Proposal further.

Sincerely,

A handwritten signature in black ink, appearing to read 'J. Sprecher', with a long horizontal flourish extending to the right.

Jeffrey C. Sprecher  
Chief Executive Officer

(Attachment)

**PART 37—EXEMPTION OF TRANSACTIONS ON A DERIVATIVES TRANSACTION FACILITY**

**§ 37.1. Definitions.**

As used in this part:

- (a) “*Derivatives transaction facility*” means any multilateral transaction execution facility (as such term is defined in § 36.1(b) of this chapter) that satisfies all of the following criteria:
- (1) None of the contracts traded or transactions conducted on or through such facility is based upon any of the commodities specifically enumerated in section 1a(3) of the Act;
  - (2) Only eligible commercial participants trading for their own account have direct or indirect trading access to such facility;
  - (3) Any and all clearing and settlement services (excluding, for the avoidance of doubt, any netting services as described in § 37.2(e) of this part) with respect to any contracts traded or transactions conducted on or through such facility are provided by a clearinghouse that is authorized by the Commission under part 39 of this chapter; and
  - (4) Such facility has been, and continues to be, recognized by the Commission as a derivatives transaction facility pursuant to § 37.3 of this part; and
- (b) “*Eligible commercial participant*” means any of the entities listed in §§ 35.1(b)(1), (2), (3), (6) and (8) of this chapter that, in connection with its business: (1) has a demonstrable capacity or ability, directly or through separate contractual arrangements, to make or take delivery of the physical commodity underlying the relevant contract or transaction; (2) incurs risks, in addition to price risk, related to the physical commodity underlying the relevant contract or transaction; (3) is a dealer that regularly provides hedging, risk management or market-making services to any of the aforementioned entities; or (4) is regularly engaged in the business of buying or selling the physical commodity underlying the relevant contract or transaction, or entering into derivative agreements, contracts or transactions in or relating to such commodity.

**§ 37.2. Contract Market Status; Exemption.**

- (a) Subject to the provisions of this § 37.2, each derivatives transaction facility shall constitute a contract market for all purposes of the Act and Commission regulations thereunder.
- (b) Each derivatives transaction facility, its operator and all contracts traded and transactions conducted on or through such facility shall be exempt from all provisions of the Act and all Commission regulations thereunder, except to the extent provided in paragraph (c) below with respect to the provisions specified therein.
- (c) Notwithstanding the exemption contained in paragraph (b) above, the following provisions shall continue to apply, but in each case only if and to the extent necessary to support the Commission's rights and authority under this part 37, including the authority to enforce compliance by a derivatives transaction facility with the core principles set forth in § 37.4 hereof: sections 1a, 2(a)(1), 4, 4b, 4g, 5a(a)(1), (2), (8), (16) and (17), 5a(b), 5b, 6(c), 9(a)(2), 9(a)(3) and 22 of the Act and §§ 1.3 and 33.10 of Commission regulations thereunder: *Provided*, That in applying any such provisions to a derivatives transaction facility, any contract traded or transaction conducted on or through such facility or any participant in such facility, such provisions will be interpreted with due regard to the different context imposed by this part 37.
- (d) For purposes of section 22(a) of the Act, a party to a contract, agreement or transaction is exempt from a claim that such contract, agreement or transaction is void, voidable, subject to rescission or otherwise invalidated or rendered unenforceable solely: (1) for failure of such contract, agreement or transaction, or the parties thereto, to comply with the terms and conditions for the exemption provided in paragraph (b) above; or (2) as a result of a violation by the relevant derivatives transaction facility of any of the provisions of this part 37.
- (e) Nothing in this part 37 shall preclude any arrangements or facilities between or among parties to any contracts traded or transactions conducted on or through a derivatives transaction facility that provide for netting of any payments or payment obligations resulting from such contracts or transactions.

**§ 37.3. Recognition; Withdrawal.**

- (a) The Commission will issue an order recognizing a prospective or existing multilateral transaction execution facility as a derivatives transaction facility for purposes of this part 37 as soon as practicable, and in any event within 30 calendar days, after a written application for such recognition has been submitted to the Commission by or on behalf of such facility. Each application

made in accordance with the foregoing sentence shall be labeled as being submitted pursuant to this part 37, and shall contain the following documents and information:

- (1) Drafts or copies of any and all (i) terms and conditions relating to trading and transacting on or through such facility, (ii) agreements entered into or to be entered into between or among any of the facility, its operator and its participants, (iii) descriptions of the trading mechanism or algorithm used or to be used by such facility, (iv) descriptions of the products traded or to be traded on or through such facility, (v) technical manuals and other guides or instructions for users of such facility and (vi) any other documents similar to those described in clauses (i) through (vi) to the extent, but only to the extent, otherwise prepared by or on behalf of such facility to be made available to its participants;
- (2) (i) Copies of any and all organizational or formation documents for such facility and any person or entity serving as its operator or in a similar capacity, (ii) a list of any and all shareholders or other holders of ownership interests in such facility, (iii) a list of the members of the board of directors or other governing board of such facility and (iv) the name of, and contact information for, the person or persons to whom the Commission may direct any notices, requests, inquiries or orders addressed to such facility; and
- (3) A written undertaking executed by an authorized representative of such facility that such facility will at all times comply with the ongoing informational requirements set forth in § 37.4(a) of this part.

*Provided*, That the Commission may issue an order of recognition pursuant to this paragraph (a) on a contingent basis if and to the extent that any of the documents or information required to be included in an application hereunder is not available at the time the application is submitted and does not become available during the 30-calendar day period following submission.

- (b) At any time after recognition of a multilateral transaction execution facility as a derivatives transaction facility, unless and until such recognition has been withdrawn in accordance with paragraph (c) or (d) below, such facility (1) may hold itself out in public as a recognized derivatives transaction facility and (2) shall disclose to its participants that any and all contracts traded and transactions conducted on or through such facility are subject to the provisions of this part 37.
- (c) The Commission may at any time issue an order withdrawing the recognition of a derivatives transaction facility if the Commission can demonstrate that



such facility, (1) in applying for recognition pursuant to paragraph (a) above, withheld any documents or information required to be included in such application or (2) fails to comply with any of the ongoing obligations and requirements set forth in §§ 37.4 and 37.5 of this part: *Provided*, That the Commission may, in its discretion, first afford such facility an opportunity to cure such failure to comply.

- (d) A recognized derivatives transaction facility may at any time withdraw from such recognition by filing a written request to such effect with the Commission at its Washington, D.C. headquarters. Any such request shall become effective immediately upon receipt by the Commission.
- (e) Any withdrawal of recognition as a derivatives transaction facility pursuant to paragraph (c) or (d) above shall not affect any action taken or to be taken by the Commission based upon actions, activities or events that occurred during the time that the relevant facility was recognized as a derivatives transaction facility by the Commission.

#### **§ 37.4. Core Principles**

To the extent applicable or appropriate with respect to any derivatives transaction facility, such facility shall at all times comply with the following core principles:

- (a) Disclose to the Commission, to the extent applicable, any material terms and conditions, agreements, trading mechanisms or algorithms, product descriptions, technical manuals and other documents of a type specified in § 37.3(a)(1) of this part, including any material amendments, supplements, revisions or updates with respect thereto, in each case at the times and to the extent, but only to the extent, that such documents or information are made available by such facility to its participants;
- (b) Monitor compliance with and enforce, to the extent applicable, the terms and conditions, agreements, trading mechanism or algorithm, product descriptions, technical manuals and other documents referred to in § 37.3(a)(1) of this part and paragraph (a) above;
- (c) If and to the extent appropriate in light of the contracts traded and transactions conducted on or through such facility:
  - (1) Monitor such trading and transactions on a routine and non-routine basis and take any measures required to ensure orderly trading; or
  - (2) Provide the Commission with such information as may from time to time be requested by the Commission to enable it to satisfy its obligations under the Act;

- (d)
  - (1) Provide to its participants on a fair, equitable and timely basis information regarding prices, bids and offers and any such other information as may be appropriate in light of the contracts traded or transactions conducted on or through such facility; and
  - (2) If and to the extent required for purposes of price discovery with respect to the underlying cash market, make available to the public information regarding settlement prices, volume, open interest, and opening and closing ranges for any actively traded product;
- (e) If and to the extent appropriate, implement and enforce fitness standards for individuals that (i) are acting as members of the board of directors or other governing board, senior executives or operators of such facility, (ii) make disciplinary determinations, if applicable, with respect to such facility's participants or employees or (ii) hold 10% or more of the shares or other equity interests in such facility; and
- (f)
  - (1) Keep full books and records of all activities related to its business as a derivatives transaction facility, including an inventory of terms and conditions and their effective dates, as well as full information relating to data entry and trade details sufficient to reconstruct trading, and any and all agreements entered into with its participants, including foreign participants, all in a form and manner acceptable to the Commission, for a period of five years, during the first two of which such books and records must be readily available; and
  - (2) Make any of the books and records described in clause (1) above available for inspection by the Commission or the U.S. Department of Justice upon request.

**§ 37.5. Other Obligations**

Each derivatives transaction facility shall at all times comply with the following additional obligations:

- (a) Upon special call by the Commission, provide to the Commission such information related to its business as a derivatives transaction facility, including information relating to data entry and trade details, all in the form and manner and within the time period specified in such special call; and
- (b) Upon request by the Commission, furnish to the Commission a current list of individuals then subject to such facility's fitness requirements in accordance with § 37.3(e) of this part.

**§ 37.6. Delegation of Authority**

The Commission hereby delegates, until the Commission orders otherwise, the authority to make special calls for information pursuant to § 37.5(b) of this part to the respective Directors of the Division of Economic Analysis and the Division of Trading and Markets, to be exercised by each Director individually or by such other employee or employees as each Director individually may designate from time to time. The respective Directors of the Division of Economic Analysis and the Division of Trading and Markets may submit to the Commission for its consideration any matter that has been delegated pursuant to this § 37.6. Nothing in this § 37.6 shall preclude the Commission from exercising the authority delegated in this paragraph at any time and in its sole discretion.