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COMMENT

April 22, 1998

Jean W. Webb, Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: Proposed Rule 140.99 Regarding Requests for Exemptive, No-Action, and Interpretative Relief

Dear Ms. Webb:

The Committee on Commodities and Futures Law (the "Committee") of the New York State Bar Association (the "Bar Association") is pleased to have the opportunity to comment on the Commission's notice of proposed rule making concerning requests for exemptive, no-action, and interpretative letters published in the January 22, 1998 Federal Register (Vol. 63, No. 14). We offer the following comments on this proposal to add a new Section 140.99 to Part 140 of the regulations ("Proposed Rule").

The Bar Association is comprised of approximately 60,000 attorneys licensed to practice in New York, and the Committee is comprised of 50 attorneys in private practice, government, corporations, and academia. They represent or have an interest in commodity and derivatives industry institutions and individuals, including futures commission merchants, floor brokers, floor traders, customers, commodity pool operators, commodity trading advisors, banks, investment banks, and commercial operators in the cash and futures business. The views expressed in this comment letter are those of the Committee and should not be imputed to the Association as a whole.

In general, we commend the Commission's attempt to establish uniform procedures for no-action letters and other requests for relief. We understand that the Commission now believes that the absence of such procedures has in the past placed a needless burden on the Commission's resources, has caused delays in the process, and has created the risk of inconsistent responses from the Commission staff. We therefore agree that the development of standard guidelines may be beneficial both to the Commission and to industry participants.

We are concerned, however, that the Proposed Rule will place additional burdens on persons requesting relief and ultimately discourage the use of the no-action, exemptive and interpretative processes. We do not believe that this result would be beneficial either to the Commission or industry participants, and we therefore recommend that the Proposed Rule be modified to reflect the comments expressed below.

The proposing release notes that the Securities and Exchange Commission ("SEC") has long required conformity with certain procedures by persons requesting no-action or interpretative letters. More particularly, in the cited 1971 release, the SEC stated that a request for no-action relief must (a) indicate the specific subsection of the particular statute to which the request pertains; (b) state the name of the companies involved; (c) address the particular transaction at hand, rather than every possible type of situation that might arise in the future; (d) contain all of the facts necessary to reach a conclusion in the matter, yet remain concise and to the point; and (e) indicate why the writer thinks a problem exists, his/her own opinion in the matter, and the basis for this opinion.[1] These requirements are quite similar to those found in paragraph (b) of the Proposed Rule, and are not problematic. As the proposing release indicates, paragraph (b) appears to be designed merely to codify existing practices, such as the Commission's refusal to provide responses to requests based on hypothetical situations or submitted on behalf of anonymous persons.[2] Similarly, the information requirement listed in sections (1), (2), (4), (6), and (7) of paragraph (c) of the Proposed Rule seeks merely procedural information and is unexceptional.

A closer comparison, however, of the Proposed Rule with the SEC guidelines indicates that significant differences exist

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[1] Securities Act Release No. 5127, 36 Fed. Reg. 2600 (January 25, 1971).

[2] See 63 Fed. Reg. 3285, 3286 (January 22, 1998).

between the two procedures. Foremost among these differences is that the SEC's procedures are set forth as guidelines, rather than rules. To the best of our knowledge, the features of the Proposed Rule described below are unprecedented among agencies issuing no-action, exemptive, or interpretative relief.[3] While we appreciate that this rulemaking has provided a vehicle for public comments, we believe that the Commission can achieve its goal of a more structured and predictable no-action process without adopting the rigidities of federal rules which even the Commission, we suspect, may someday find to be troublesomely inflexible. We believe that these procedures will increase, rather than diminish, the burdens imposed on Commission staff and requesting parties, and will serve only to discourage the submission of requests for relief.

In this regard, we note that the proposing release indicates that the Commission intends the Proposed Rule to reduce the number of requests and direct Commission actions toward the rulemaking process:

> "The Commission believes that the best mechanism for handling novel or complex issues, significant gaps in regulatory coverage, relief from regulatory requirements or initiatives for regulatory reform generally is the notice and comment rulemaking process or, where appropriate, exemptive action by the Commission itself after notice and public comment."[4]

Indeed, the Commission staff already appears to be implementing this approach.[5] We respectfully submit that the no-action, exemptive, and interpretative processes have developed an effective means of addressing issues arising under the CEA and the Commission's rules without the burden and delays involved in the rulemaking process. The relief process, as it now exists, also fosters a valuable dialogue between the Commission and industry participants; as a catalyst for interaction, it increases the Commission's awareness of new business developments while simultaneously facilitating commercial activities with minimal

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[3] Neither the SEC, the Federal Reserve Board, nor the Office of the Comptroller of the Currency imposes procedures similar to those discussed below.

[4] See 63 Fed. Reg. at 3285.

[5] See Interpretative Letter 98-02.

disruption.

We are concerned that the proposal seeks to apply identical standards to requests for different types of relief, ranging from no-action letters through interpretations to exemptions, and regardless of whether the relief is sought from the staff or the Commission. These types of relief vary in their legal and policy implications, and it would seem reasonable to approach a potential Commission interpretation or exemption, for example, with a higher degree of formality than a staff no-action letter. However, the proposed rules posit a "one size fits all" approach that we believe is particularly onerous when applied to everyday no-action letters.

We are also concerned that the distinction between "routine" issues, on the one hand, and "novel and complex", on the other, may not be so easily perceived by the Commission staff, and that matters that generally are regarded as routine by many might be assigned to the "novel and complex" bin. Recent experience has suggested that this is a real risk.[6] Thus, matters that should be handled expeditiously by the granting of no-action relief could become enmeshed in a lengthy and expensive rulemaking process, and both the requesting party and the Commission will have their burdens increased.

We believe that, rather than proceed with changes that could restrict the utility of no-action or other relief, the Commission should consider utilizing some of the same mechanisms that the SEC has adopted to lighten the burden upon its staff. For instance, in 1994 the SEC staff developed a new practice to deal with the multitude of no-action requests under the SEC's new Section 16 rules: Each requestor faxes to the staff a "talking points" memorandum briefly describing the requestor's position on the issues without identifying the client.[7] Within a few days, the staff indicates orally whether it is inclined to agree or disagree with the requestor's position on the various issues. This enables the staff to allocate its time between those proposals requiring more serious evaluation and those that merely present minor variations on transactions that the staff has previously addressed. While this may not be an effective mechanism for novel or particularly complex issues, it could help relieve the burden for more routine requests that the Comm-

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[6] See footnote 5, supra.

[7] For a discussion of this system, see Richard H. Rowe, "Reliance on SEC Staff 'No Action' Letters - A Shield or Sword?", 896 PLI/Corp 667 (June 1995).

ission's staff must address.

Yet another more flexible approach would be to issue a "guidance" release (perhaps by the Division of Trading and Markets and/or the Office of the General Counsel) concerning requests for no-action, exemptive, and interpretative relief. Such guidelines could provide the Commission staff with discretion to demand some of the stringent filing requirements in specified circumstances or in circumstances deemed appropriate by the Commission staff. Where possible, the guidelines should encourage a minimum submission of material. A release of this nature could be augmented by guidelines for internal use at the Commission. These internal guidelines should be tailored to achieve efficiency, consistency, and clarity of response.

We understand that the Commission staff has indicated that it will still accept draft submissions and will engage in informal discussions regarding no action letters and other requests for relief prior to a submission pursuant to Rule 140.99. We support that position and suggest that the Federal Register release containing the final rule make this point clearly.

Set forth below are our comments on specific provisions of the Proposed Rule.

1. Reliance on No-Action and Other Relief.

Under the Proposed Rule, no-action letters will be effective only with respect to the person or persons to whom they are addressed, while interpretative letters may be relied upon by third parties.[8] This distinction contrasts with the prevailing view that no-action letters, while directly applicable only to the addressees themselves, provide guidance as to the Commission's views on the matters at issue. While we do not suggest that these letters should bind the issuing Division vis-a-vis third parties, neither should their value as guidance to other parties be entirely eliminated. We recommend that the Commission make clear that, while no-action letters bind only the staff and may be relied upon for this purpose only by the addressee, they may nonetheless be relied upon as guidance by third parties.

The Proposed Rule also indicates that interpretative letters will be binding solely on the Division issuing them, not

[8] See 63 Fed. Reg. at 3286.

on the Commission as a whole, nor on any other Division.[9] If, as the proposing release states, a purpose of the Proposed Rule is to avoid inconsistent staff responses, an interpretative letter should bind all Divisions -- at least until the Commission acts, or the interpretation is modified prospectively. In particular, under the Proposed Rule, the Division of Enforcement would be free to ignore an interpretative letter issued by the Division of Trading and Markets; an interpretative letter that was so limited would offer little (if any) comfort.

Ordinarily, interested parties will understandably rely on such relief and expect that the Divisions will have consulted with each other on important issues before issuing relief. Accordingly, the expression and implementation of contrary views of non-issuing Divisions will be disruptive and inequitable. Though we understand the view that staff letters do not necessarily bind the Commission itself, we are concerned that the possible divergence of views among staff and the delays associated therewith might discourage industry participants from using the interpretative letter process. We therefore recommend that this restriction be eliminated.

2. Citations to Authority.

Sections (5) and (6) of paragraph (c) of the Proposed Rule would require that requests make reference to "all relevant authorities" and "identify and distinguish all adverse authority."[10] The meaning of the phrase "all relevant authority", however, is unclear. For example, "adverse authority" could be construed to encompass any prior denials of relief in similar situations, or previous letters that imposed additional or different conditions. Given this lack of a clear definition, we anticipate that requesting parties will err on the side of caution and include all precedents that might possibly be relevant to their requests, which would result in increased labor for the staff, as well as the requesting parties.

Of course, as a practical matter, parties seeking no-action relief traditionally cite other examples where comparable relief has been granted, and note any relevant distinctions, as well as any different conditions attached to such relief. Similarly, parties submitting requests to the SEC generally include discussions of previous no-action letters concerning similar transactions or circumstances, even though such discus-

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[9] See 63 Fed. Reg. at 3288.

[10] See 63 Fed. Reg. at 3286.

sion is not technically required by the SEC. The key distinction reflected in the Proposed Rule is that the Commission's staff would be able to reject a request simply because, in the staff's view, the request failed to cite or distinguish all adverse authority.

While we believe it is reasonable and beneficial to require, as the SEC does, that a request provide a thorough discussion of the situation at issue and the requesting party's reasoning as to why the request should be granted, we do not believe that full presentation of the issues requires a brief of the type used in a litigation context. Such a requirement would certainly increase the burden on those seeking relief, while there is no reason to believe that it would substantially diminish the time spent by Commission staff in handling requests.

As a practical matter, many requestors do not have the library or staffing resources to provide the kind of exhaustive research and presentation the Proposed Rule appears to require. An additional problem is that it is only relatively recently that the Commission has implemented a policy to publicly disclose all no-action letters. To reject requests from such parties solely because of a perceived research inadequacy would be inequitable. Moreover, the "chilling" effect of such harsh requirements would deprive the Commission staff of the benefit of dialogue and interaction with that segment of the industry.

In the past, the no-action process has been praised as a model of efficient interaction between government and industry, and compared to an alternative dispute resolution forum where the two sides can resolve their differences through negotiation.[11] The requirement that a request cite and distinguish all adverse authority threatens to turn the process into a more cumbersome and adversarial one and thus eliminates many of the benefits that have developed over time. We recommend that requesting parties be required only to discuss relevant precedents.

3. "Hypotheticals".

Section 140.99(b)(5)(ii) makes clear that the staff will not respond to a request based upon a hypothetical situation. While the Committee accepts this notion, it believes that the concept of "hypothetical" may be used to exclude bona fide alternatives that industry participants are seeking to utilize to

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[11] See, e.g., Richard H. Rowe, "A SEC 'No-Action' Position: An Impervious Shield or a Paper Tiger?" 6 No. 7 Insights 21 (July 1992).

solve a problem or take advantage of a market opportunity. On occasion in the past products have been developed with alternative formats. The adopting release, or indeed the final rule, should make clear that requestors may present the staff with alternatives or permutations without risking the rejection of the request on "hypothetical" grounds.

The Notice of Proposed Rulemaking also suggests that the Commission will not accept requests for relief pertaining to ongoing business activity. While we agree that such requests may present special difficulties and issues, there are situations where ongoing conduct is an appropriate subject of a request, and the Commission and its staff should have the flexibility to address those situations. For example, a new court decision or Commission interpretation issued to another party may raise issues that were not apparent or significant when business activity was initiated, and make seeking Commission guidance or relief advisable. The Commission and its staff have addressed such situations in the past, and should continue to do so when warranted. If the Commission is concerned with granting no-action relief to past conduct in reliance on a letter request that cannot convey all possible facts and circumstances that might be deemed relevant, it can, as the staff has done in the past, issue relief that specifically excludes past conduct and can be relied on only as to conduct occurring after the relief is issued.

4. Electronic Filing and Abbreviated Responses.

The Notice of Proposed Rule making requests comments on whether the rule should permit requests to be filed electronically and whether an abbreviated response procedure should be utilized.[12] The Committee believes that both are desirable. While the Committee recognizes that abbreviated responses are not always appropriate, there will be times when they will be effective. In those circumstances, an abbreviated response will be likely to save staff resources and speed the relief, both desirable goals.[13] Moreover, if the Commission does not permit abbreviated responses, what has been a lengthy process in the past could become even worse under the proposed filing require-

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[12] See 63 Fed. Reg. at 3286 and 3287.

[13] The Committee believes that the Commission should make public incoming request letters as well as its responses. This would obviously be necessary with the implementation of abbreviated responses. Needless to say, the identity of the party making the request could be deleted.

5. Withdrawal of Requests.

We are also concerned that paragraph (f) of the Proposed Rule, which severely limits the ability of a party to withdraw a request for relief, will have a "chilling" effect on the use of the no-action, exemptive, or interpretative procedures. In the past, persons seeking no-action relief have had the option of withdrawing their requests for various reasons, e.g., a request might be withdrawn if the requesting party determined that the relief was no longer needed because the circumstances had changed or because a precedent issued subsequent to the request suggested that relief was no longer necessary.

Under the Proposed Rule, however, a request could be withdrawn only in limited circumstances, i.e., that the person making the request has decided not to proceed with the proposal or that intervening events have made the request moot. From the example given in the proposing release, it appears that the latter exception applies to factual, not legal changes, and would not cover the case where the publication of interpretative relief with respect to a third party suggested that relief was unnecessary.[14]

The structuring of the CFTC's approach could be utilized by the staff to reject inquiries, and thus to make law, without the benefit of public exposure and comment, by either negative responses or by the uncertainties associated with delay (there is no commitment in the release or the proposed rules to have the staff act promptly) or unclear responses. The limited rights of withdrawal may reinforce this concern. By contrast, the SEC rarely issues negative responses, instead permitting requesting parties to withdraw and to go back to the drawing board. If after getting negative indications a company nevertheless proceeds (typically with some tweaking), it proceeds at its peril, and everyone understands that. It should not be necessary to promise the staff that the company will let matters die.

Under the Proposed Rule, a person requesting relief would not be able to implement a proposal until the staff makes a decision. Because the Proposed Rule does not impose any time limits on the review of requests, a proposal might remain stalled for extensive periods of time, which could render it impossible to proceed with its implementation. Effectively, the staff could deny relief by merely delaying its review. Because of these potential problems, the likely consequence of the adoption of the

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[14] See 63 Fed. Reg. at 3287.

Proposed Rule, in our view, would be a dramatic reduction in the use of the no-action, interpretative, and exemptive process.

6. Certification.

Proposed Rule 140.99(c)(3) requires certification of the "statements contained" in the requesting letter by someone with "knowledge of the facts."[15] We believe that this requirement is unwarranted. Common sense makes clear that a requesting party cannot rely on relief granted on the basis of a material misrepresentation or omission. Moreover, attorneys, who we suspect do the bulk of the submissions, already have a professional, ethical obligation to submit accurate information. See, e.g., Part 14 of the Commissions regulations. If, however, the Commission implements this requirement, the Committee believes that the certification should be made by the client, or the party-in-interest, and that it should relate only to the facts in the request, not the other "statements." We recommend that the rule, and the issuing release, be amended to clarify this point.

This section also requires that the certifying party undertake to advise the Commission staff of any material changes in circumstances, including those occurring after relief is granted. This requirement should not rest on the shoulders of counsel, but instead should be the responsibility of the principal or party-in-interest. There is simply no way for counsel, especially outside counsel, to track and keep current with respect to factual matters bearing on the request and any relief received.

The requirement also creates a legal liability, independent of the risk of Enforcement Division action against the client, for conduct outside the scope of the relief granted. Of course, there is an obligation to update facts during the pendency of the request (which does not pose a problem), but once the request is made, there is an obligation by rule, under threat of enforcement, to keep the Commission advised of developments, even after relief is granted. And there is no time period specified as to when this obligation ceases. Such exposure will tend to deter interested parties from utilizing the no-action process.

We also recommend that any final rule acknowledge that the Commission has implemented a policy to publish all grants or denials of requests for no-action, interpretation, or exemptive relief. We understand that this is, in fact, the Commission's

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[15] See 63 Fed. Reg. at 3288.

current practice, and has been for a number of years. However, in the past, some staff letters were not published or otherwise released, and the Commission should take steps to ensure that all such responses are available to the industry and the public. As is currently the practice, redacted versions can be released when appropriate to protect the identity of requesting parties and to preserve the confidentiality of information.

CONCLUSION

In general, therefore, while we support the Commission's effort to streamline the relief process and better utilize its scarce resources, we believe that the codification of procedures as contemplated by the Proposed Rule does not represent an adequate solution to these problems, and may in fact impede the process. In this regard, we note that neither the Federal Reserve Board nor the Office of the Comptroller of the Currency, both of which are often called upon to respond to requests for relief, have adopted any of the provisions about which we have expressed concern. We recommend that the Proposed Rule be modified as suggested above.

The Committee has also reviewed the comment letter of the Futures Law Committee of the Association of the Bar of the City of New York and concurs in the comments and views expressed therein to the extent they are not inconsistent with the views we express here.

We appreciate the opportunity to comment on the Proposed Rule and would be pleased to discuss these issues further with the Commission or its staff. Please call me at (212) 545-1900 if you have any questions or if we can provide assistance in connection with the Commission's consideration of the Proposed Rule.

Sincerely yours,

Samuel F. Abernethy
Chair

SFA/ed