

August 3, 2005

Via E-Mail

Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

OFFICE OF THE SECRETARIAT

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C.F.T.C.

Re: Rule Certification. NYMEX Submission 05.135: Notification of Amendment to COMEX Rule 104.36, Exchanges for Physicals.

Dear Ms. Jean Webb:

The New York Mercantile Exchange ("NYMEX" or the "Exchange") is notifying the Commodity Futures Trading Commission ("CFTC" or "Commission") of an amendment to COMEX Rule 104.36, Exchanges for Physicals.

The amendment to COMEX Rule 104.36 and accompanying commentary prohibits Exchanges for Physicals ("EFPs") made "in connection with" offsetting physical transactions during RTH. The previous reference in the rule to "contingent" physical transactions was removed in response to the Division of Market Oversight's concern that the language in the Rule inadvertently implied that contingent transactions are permissible at times other than RTH. This amendment will be effective as of Monday, August 8, 2005. Pursuant to Section 5c(c) of the Commodity Exchange Act ("Act") and CFTC Rule 40.6, the Exchange hereby certifies that the attached rule amendment complies with the Act, including regulations under the Act.

Should you have any questions concerning the above, please contact Nancy Minett, Vice President, Compliance, at (212) 299-2940.

Very truly yours,

Nancy M. Minett
Vice President
Compliance Department

cc: Brian Regan
Thomas LaSala

(Underlining in bold indicates additions; strikethroughs in bold indicate deletions.)

COMEX Rule 104.36, Exchanges for Physicals, and Associated Interpretation

(a) General Rule. An exchange of physical commodities for futures contracts ("EFP") shall be permitted by arrangement between members in accordance with the requirements of this Rule.

(b) Parties to an EFP. An EFP may be consummated between two parties if one of the parties is the buyer of the physical commodity and the seller of the futures contract, and the other party is the seller of the physical commodity and the buyer of the futures contract.

(c) Simultaneity of Transfer. The purchase and sale of the futures contract shall be simultaneous with the sale and purchase of an equal quantity of the physical commodity.

(d) Ownership of Commodity. The seller of the physical commodity must have either possession or a contractual right to future possession of the physical commodity at the time of entry into the EFP. In the case of an EFP transacted at any time in which the Exchange offers trading in its contracts during the business day, the transfer of the physical commodity by means of the EFP may not be ~~contingent upon~~ **made in connection with** an offsetting cash commodity transaction.

(e) Equivalent Physical Commodities. For purposes of this Rule, the physical commodity (1) need not comply with the specifications therefore contained in the futures contract which is being exchanged, but need only be substantially the economic equivalent thereof, and (2) may not be a futures contract or a contract for future delivery traded on a "designated contract market" as that term is used and defined under the Act.

(f) Price of EFP. An EFP may be transacted at such prices as is mutually agreed upon by the two parties to the EFP.

(g) Reports and Recordkeeping.

(1) Each EFP entered into during regular trading hours shall be reported to an Exchange employee designated for that purpose by no later than the close of regular trading hours on the day the transaction is effected. Each EFP entered into after the close of regular trading hours and prior to the opening on the next business day shall be reported to an Exchange employee designated for that purpose by no later than 10:00 a.m. on such next business day. Such report shall specify the seller of the futures contract and the number of contracts involved in the EFP.

(2) Each order ticket prepared by a member or member firm in connection with an EFP transaction and all trade data submitted to the Exchange to match and clear an EFP shall specially identify the transaction as an EFP.

(3) (A) Each member or member firm which has entered into an EFP for its own account shall maintain full and complete documentation (including, but not limited to, the time of entry) of the EFP and any cash commodity transaction related thereto.

(B) Each member or member firm which has reported or cleared an EFP on behalf of a customer shall provide to the Exchange such documentation of an EFP and any cash commodity transaction related thereto as the Exchange may request.

Interpretation of the Governors Committee of Commodity Exchange, Inc. Regarding Exchanges of Futures for Physicals ("EFP")

Essential Elements and Other Indicia of a Bona Fide EFP

The Board has identified the following as essential elements of an EFP transaction:

(1) There must be both a cash transaction and a futures transaction, which transactions must be integrally related.

(2) The cash commodity contract must provide for a transfer of ownership of the cash commodity to the cash buyer upon performance of the terms of the contract, with delivery to take place within a reasonable period of time thereafter in accordance with prevailing cash market practice (subject, of course, to the buyer's obligation to pay for the commodity). Actual delivery need not take place should the selling party offset that obligation by other means.

(3) There must be separate parties to the EFP -- that is, the accounts involved must have different beneficial ownership or be under separate control.

The Governors Committee has resolved that every EFP transacted on COMEX must satisfy the above-identified essential elements. In addition, the Governors Committee has developed a more inclusive list of other indicia to be considered, in conjunction with Rule 104.36, as a basis for determining whether the essential elements of an EFP have been satisfied in evaluating the bona fides of a particular transaction:

- (a) The degree of price correlation between the cash component and the futures contract.
- (b) The prices of the futures and cash legs of the EFP and their relation to the relevant prices in either market.
- (c) Whether the seller has possession, the right to possession, or the right to future possession of the cash commodity prior to the EFP.

The criteria for a bona fide EFP were taken verbatim from The Report on Exchanges of Futures for Physicals, at pages 146-147, 150-151, 192-193 and 195-196. Any reader interested in an expanded explanation of these criteria should see The Report.

- (d) The cash seller's ability to perform on his delivery obligation in the absence of prior possession of the cash commodity (i.e., the cash seller's access to the cash market).
- (e) Whether the cash buyer acquires title to the cash commodity.

Ownership of the Physical Commodity

Questions have arisen as to the permissibility of an EFP involving the transfer of a physical commodity **which is contingent upon in connection with** the consummation of an additional cash commodity transaction offsetting the cash commodity component of the EFP. For example, a trader may purchase the cash commodity and upon condition that he can immediately resell it to the person from whom it was purchased in exchange for a long futures position (or, conversely, the trader may sell the cash commodity and repurchase it together with a short futures position) by means of an EFP. Alternatively, a trader may transact an EFP with one party as a condition to entering into a cash commodity transaction with another party, which will liquidate the cash commodity component of the EFP.

The Board has determined to bar the use during COMEX trading hours of EFPs such as those described above **which involve contingent ownership of the cash commodity**, as such activity appears to be undertaken with the primary intent of avoiding open and competitive trade execution when entering or exiting the futures market. Accordingly, no EFP which is linked to **or contingent upon** entry into a second, offsetting cash trade may be transacted during COMEX's business hours at any time that COMEX offers trading in its contracts, unless trading in a market is halted, such as during a physical emergency.

Recordkeeping

COMEX requires that members and member firms who participate in and clear EFPs keep full and complete records of all such transactions, and also be in a position to provide records for any EFP transaction which they clear on a give-up basis. Complete records have been deemed to consist of the following documents, or their equivalents, if applicable: account statements, sales invoices, delivery instructions to a depository or dealer, confirmations from a depository or dealer showing delivery and receipt of payment, and, if available, physical inventory records. The Exchange also requires that members and member firms keep and/or be in a position to provide full and complete records of any and all cash commodity transactions executed in combination with an EFP which effect the offset of the cash commodity component of the EFP. With respect both to the EFP as well as any related cash commodities transaction, records must include documentation of the time at which the parties entered into each such transaction.