July 15, 2003

VIA FACSIMILE, E-MAIL AND EXPRESS MAIL
Ms. Jean A. Webb
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Request for Amendment to May 30, 2002 Commodity Futures Trading Commission Order Concerning Customer Funds Held for Clearing of Off-Exchange Transactions in Contracts Listed Only for Clearing by NYMEX

Dear Ms. Webb:

The New York Mercantile Exchange, Inc. ("NYMEX" or the "Exchange") requests that the Commodity Futures Trading Commission ("CFTC" or "Commission") amend on a temporary basis a May 30, 2002 Commission order. That order concerns the treatment of funds held in connection with the clearing of certain products executed off-exchange in over-the-counter ("OTC") markets and cleared as futures by the Exchange ("Section 4(d) Order").

The Exchange requests that the Section 4(d) Order be amended on a temporary basis until NYMEX ClearPort(sm) Trading, the Exchange's newest electronic trading system, can be enhanced through the addition of new functionality for the listing and trading of options contracts on the system. NYMEX staff currently anticipates that such enhancements should be implemented in November 2003.

Specifically, as further described below, NYMEX requests that the Section 4(d) Order be amended in two ways. First, we request that the Section 4(d) Order be amended to include four new contracts to be listed by the Exchange only for clearing using the Exchange's ClearPort(sm) Clearing website services. Second, the Section 4(d) Order currently tracks the scope of NYMEX's submission and thus refers only to submission of transactions executed off-exchange that are submitted to the Exchange using the established exchange of futures for physicals or exchange of futures for swaps procedures; consequently, we request that a conforming amendment be made to the Section 4(d) Order to acknowledge that these options transactions would be submitted to the Exchange via an exchange of OTC options for Exchange options ("EOO") procedure.

As a note, the Exchange first implemented an EOO rule several years in the wake of the Enron meltdown. A copy of the current EOO rule, which specifies the Exchange's existing procedures and safeguards, is included as an attachment to this letter. (In conjunction with the Commission's amendment of the Section 4(d) Order, the Exchange intends to self-certify a few technical changes to this rule to reference submission of EOO transactions via the Exchange's website.)

The Exchange's existing clearing services for transactions executed off-exchange have clearly responded to a real business need for mitigation of counterparty credit risk for OTC transactions, and, over the last year, our clearing services have achieved a substantial level of acceptance and usage by the business community. We continue to be very appreciative of the Commission's open-mindedness and cooperation on new market developments. Based upon feedback from current and potential users, it is our understanding that this credit mitigation service is also critically needed for OTC energy options markets as well.

Each of the four new contracts to be listed only for clearing at the Exchange are modeled upon option contracts trading in OTC contracts that are essentially OTC "look-alike" versions of existing NYMEX option contracts in crude oil, heating oil, unleaded gasoline. Copies of the terms and conditions rules chapters for each of these four new option contracts are included as attachments to this letter.

In essence, the look-alike products trading in OTC markets that are based upon existing NYMEX floor-traded option contracts differ from those floor-traded contracts in only two respects. First, the OTC look-alikes provide for European exercise. As the Commission knows well, European exercise only permits exercise on the expiration date. By contrast, the Exchange's current floor-traded option contracts allow for American exercise, which can be exercised at any time prior to or on the expiration date. Second, the OTC look-alikes only provide for cash settlement; by comparison, the Exchange's current floor-traded contracts can be exercised to buy or sell a futures contract.

Consequently, the four new option contracts to be listed by the Exchange only for clearing through NYMEX ClearPort(sm) Clearing are all European-exercise cash-settled contracts. In all other respects, the terms of these news option contracts are the same as the Exchange's established floor-traded option contracts. In other words, the underlying contracts for these new option contracts really are the regulated futures contracts traded on the Exchange. While the size of the underlying OTC markets vary somewhat by commodity, each of the new NYMEX option contracts is modeled upon an OTC look-alike option contract that has a reasonably liquid OTC market. Indeed, in some instances, such as for the natural gas look-alike option contract, trading volume in the OTC option product may well exceed trading volume in the Exchange's floor-traded option product.

The Exchange intends to list 72 consecutive contract months for the natural gas look-alike option contract, which is the same number of contract months listed for the corresponding Exchange floor-traded option contract. For the other three contracts, the Exchange would list the same number of contract months as are listed for the underlying futures contracts. Thus, the Exchange would list 18 consecutive months for the heating oil look-alike option contract. For the crude oil look-alike option contract, the Exchange would list 30 consecutive contract months, then list quarterly contract months for the following twelve months, followed by listing of a December contract month for the next four years. With regard to unleaded gasoline, the Exchange normally lists twelve consecutive contract months for the futures contract but presently only has nine contract months listed because of market uncertainty relating to New York State's looming ban on MTBE.

In addition, the Exchange intends to list the same strike price intervals for the new option contracts as are available for the floor-traded option contracts. As is the case with floor-traded option contracts, Exchange technology systems will have the flexibility to add strike price interval on an intra-session basis. (Under rules that were approved by the Commission several years ago, strike prices can be added on a same-day basis so long as the Exchange files notice of such changes with the Commission within three business days of the listing of the new strike price.)

As a note, the Exchange does not intend to list FLEX options as part of this new service. FLEX options may be generally characterized as options involving any strike price, any expiration date and any contract month. While there would be flexibility regarding the strike prices to be listed, the Exchange does not intend to provide the same level of flexibility for expiration dates and contract months. With respect to exercise and assignment procedures, as noted above, each of the four new option contracts would be limited to cash settlement and thus would not necessitate detailed exercise or assignment procedures.

Settlement prices will be obtained from a Black European option pricing model, which is the current industry standard for pricing of European option products, and Exchange staff will use the same volatilities associated with the respective floor-traded option contracts. Margins will be set using the SPAN margin system. While Exchange staff presumes that the Commission and Commission staff are very familiar with SPAN by this point in time, as a convenience, we have included as a separate attachment some general information on this margining system. As a technical note, it is the understanding of Exchange staff that the SPAN system already uses the European model for calculating margin on all products covered by that system. In this regard, with respect to use of risk arrays for the SPAN margining system, the underlying futures margin will be used to determine risk arrays, along with the floor-traded volatility scan range. Furthermore, as these new products are in effect options on futures contracts, the products will be marked to market using the Black European option pricing model with parameters derived from respective floor-traded options. These parameters include term and strike price volatility skews.

By separate letter, the Exchange is also submitting a request to amend a January 29, 2003 CFTC order ("Locals Order") in order to permit NYMEX floor members who have the necessary FCM guarantee to be able to enter into OTC option transactions that will be cleared on the Exchange. The Exchange would prefer for the Locals Order to be amended concurrently with, or as soon as practicable following, amendment of the Section 4(d) Order. However, the Exchange believes that amendment of the Section 4(d) Order should take precedence over amendment of the Locals Order. Therefore, Exchange staff requests that amendment of the Section 4(d) Order not be delayed by any amendment of the Locals Order.

We appreciate the Commission's consideration of this request. We look forward to working with the Commission and Commission staff on this filing, and we are prepared to work with CFTC staff on this request on an expedited basis. If you have any questions, please do not hesitate to contact the undersigned at (212) 299-2200 or contact Brian Regan at (212) 299-2207 or Robert Levin at (212) 299-2390. Please note that I will be on vacation beginning on July 18, 2003 and continuing until August 4, 2003; however, Brian Regan will be available throughout this period.

Respectfully submitted,

Christopher K. Bowen
Chief Administrative Officer and
General Counsel

cc: Chairman James E. Newsome
Commissioner Barbara P. Holum
Commissioner Walter Lukken
Commissioner Sharon Brown-Hruska
Jane Thorpe, Esq.