

2/7/08

RECEIVED  
C.F.T.C.



Atlanta Calgary Chicago Houston London New York Singapore

2008 FEB -6 PM 4:13

OFC. OF THE SECRETARIAT

February 6, 2008

David A. Stawick, Secretary  
Commodity Futures Trading Commission  
1155 21st Street, N.W.  
Washington, D.C. 20581

**COMMENT**

Re: ICE Clear US Section 4(c) Request—72 Fed. Reg. 68862 (December 6, 2007)

Dear Mr. Stawick:

ICE Clear U.S.<sup>TM</sup>, Inc. ("ICE Clear") and ICE Futures U.S.<sup>TM</sup>, Inc. ("ICE Futures") submit this letter in further support of their respective petitions to the Commission for exemptive orders under Section 4(c) of the Commodity Exchange Act, as amended (the "Act") related to the introduction of cleared-only agricultural swaps.

ICE Clear and ICE Futures are subsidiaries of IntercontinentalExchange<sup>®</sup>, a leading operator of global exchanges and over-the-counter (OTC) markets. IntercontinentalExchange offers futures and OTC markets on a single trading platform in a diverse set of products based on crude oil and refined products, natural gas, power and emissions, as well as agricultural commodities such as canola, cocoa, coffee, cotton, orange juice, wood pulp and sugar, in addition to foreign currency and equity index futures and options. It also provides clearing services for its US and Canadian exchanges through ICE Clear US and ICE Clear Canada<sup>TM</sup>. IntercontinentalExchange was added to the Russell 1000<sup>®</sup> Index in June 2006 and the S&P 500 Index in September 2007.

The relief requested by ICE Clear and ICE Futures to facilitate the clearing of OTC transactions in certain non-enumerated, agricultural commodities is fully set forth in the Petitions filed on September 11 and 14, 2007 and described in the December 6, 2007 Federal Register notice in which the Commission solicited comments. It was also a topic of discussion at the Agricultural Advisory Committee meeting held on the same date. Notwithstanding active participation as a presenter that advocated the clearing of OTC agricultural swaps at that meeting, and notwithstanding numerous statements in support of similar exemptive relief for itself, the CME Group requested an extension of the comment period so that it could "properly consider" the issues in the context of its competitors--ICE Clear and ICE Futures.

Some of the issues about which the CME seeks to inject concern are administrative matters that involve the internal procedures of the Commission but have little to do with the merits of the ICE Clear and ICE Futures requests. For example, whether the

ICE Futures U.S., Inc.  
World Financial Center  
One North End Ave  
New York, NY 10282  
phone 212 748 4000  
fax 212 742 6981  
online www.theice.com

Commission prefers to act on individual petitions on a case-by case basis or to issue a general interpretation or blanket exemption with respect to clearing OTC agricultural contracts should be a matter left to the Commission and does not affect the merits of the petitions. Moreover, approvals granted to ICE Clear and ICE Futures could be made subject to compliance with the terms of any subsequently issued blanket exemption or interpretation.

Other issues raised by the CME in its request for extension of the comment period suggest that they have not read the submissions made by ICE Clear or ICE Futures, nor their own public filings on the subject. Indeed, many involve matters about which the CME has previously (and, in some cases, recently) taken a position that supports the requested relief. These include: (I) submissions petitioning the Commission for an order pursuant to Section 4d of the Act that would prescribe terms and conditions for the commingling of customer funds used to margin OTC currency contracts with other funds held in segregated accounts ("CME Submission #05-104"), (II) submissions petitioning the Commission for an order pursuant to Section 1a(12)(C) of the Act permitting its floor brokers and floor traders to be eligible contract participants so that they can enter into OTC transactions cleared by the CME ("CME Submission #05-105"); (III) issuance of a document containing "Frequently Asked Questions" (the "FAQ") following the Commission's grant of the requested relief, which details procedures for clearing OTC transactions and highlighting its benefits; and (IV) a presentation at the CFTC Agricultural Advisory Committee meeting on December 6, 2007, which became part of the meeting record (the "2007 Presentation"). We highlight some examples below.

□ On the subject of the extent to which a cleared-only OTC agricultural swaps may be part of a fungible class of agreements that are standardized as to their material economic terms, the CME (citing a Lehman Brothers research report) stated in its own submissions that:

Swaps carry credit risk since they are subject to the default of the counterparty . . . the main drawbacks to swaps . . . is . . . non-fungibility . . . and the absence of a centralized market. When an investor wants to unwind his/her position, he/she has to either enter another swap and be exposed to two default risks or reach an agreement with the original counterparty to close the swap [thus] investing in swaps requires significant logistics [and] price transparency may be diminished . . . Going forward, we can expect the creation of a central clearing house that could alleviate these problems. Marking to market swaps will reduce the liquidity risk, and creating standardized products will improve the liquidity of the market.

**These same conditions exist in the OTC market for our agricultural commodities and the same benefits will inure to our marketplace under the ICE Clear proposal.**

□ On the subject of whether cleared-only OTC agricultural swaps are consistent with the public interest and the purposes of the Act, the CME pointed to the lack of transparency in OTC markets and the benefits that clearing would bring, as follows:

Flexibility, or the ability to tailor a contract to the risk-management needs of the moment, has long been an important benefit associated with OTC derivative markets. The deployment of the 'futures-to-the-date' concept creates additional flexibility, extending the utility of CME contracts as ECPs may more precisely hedge their cash positions with offsetting futures positions that match closely in terms of date.

In its FAQ, the CME listed the market benefits of clearing OTC transactions as follows:

- Central counterparty clearing, which offers greater capital and operational efficiencies, including risk offsets against related futures and options positions;
- World-class risk management of the credit, operational, and legal risks that customers face in OTC trading;
- Regulated market protections that institutions have come to expect

At the 2007 Presentation, it once again highlighted the "*Regulatory Benefits of Cleared Ag Swaps*" in the following way:

- Bridge unregulated OTC markets with regulated Exchange-traded markets
- Increase transparency through public reporting of volume, open interest and settlement prices
- Valuation and pay/collect for counterparties provided by Clearing House
- Enhanced market surveillance
- Backed by capital of Clearing House
- Enhanced Financial Integrity of transactions as counterparty risk is eliminated

**The same benefits would inure to agricultural market participants under the ICE Clear proposal, and the public interest and purposes of the Act would be satisfied in the same way.**

□ On the subject of the conditions under which it may be determined that cleared-only OTC agricultural swaps will not have a material adverse effect on the ability of the Commission and the relevant registered entities to discharge their regulatory and self-regulatory responsibilities, the CME answered this question by stating, in its submissions that it would

deploy the same systems, procedures, people and processes to clear SUB transactions as currently utilized with other transactions cleared by CME.

**ICE Clear intends to use its same systems, procedures, people and processes to clear its "cleared only" futures contracts as currently utilized by it with other transactions it clears.**

□ On the subject of identifying the necessary requirements with respect to the liquidity of the underlying markets or how the risk of a potential default with respect to cleared-only OTC agricultural swaps should otherwise be mitigated, the CME addressed the question of liquidity requirements for "to-the-date" contracts and the default risk in its own submissions, as follows:

CME intends to apply standard margining levels to cleared only futures despite the likelihood that liquidity in these contracts may be diminished relative to traded and cleared futures.

It went on to note that risk could be laid off either in the relevant OTC market or

in its own regularly listed currency and interest rate contracts. CME does not anticipate any particular operational problems associated with such risk-management activity to the extent that any such activity in the context of [cleared only] futures . . . is completely analogous to risk management activities associated with standard IMM-dated contracts, for which the CME Clearing House is well prepared. Accordingly, these dynamically-listed futures . . . shall be subject to normal CME margin requirements and to applicable CME Rules and CFTC Regulations.

**ICE Clear will also apply standard margining levels and have recourse to the OTC markets, as well as the ICE Futures listed contracts to which the cleared-only swaps correlate.**

□ On the subject of the conditions under which funds used to margin cleared-only OTC agricultural swaps should be permitted to be commingled with funds held in segregation, the CME petitioned the Commission for an order pursuant to Section 4d of the Act that prescribed terms and conditions for the commingling of funds used to margin OTC currency contracts with other funds held in segregated accounts. It then touted the advantage of the bankruptcy laws by stating as follows:

Moreover, customer collateral deposited with CME for cleared futures is segregated and protected from a bankruptcy in the carrying clearing member's proprietary origin.

In its 2007 Presentation, the ability to commingle such funds was again emphasized as one of the benefits of clearing OTC agricultural swap transactions, in a segment titled *"Market Benefits of Cleared Ag Basis Swaps With Margins Held in Customer Segregated Account*, as follows:

- Enhanced risk management for agricultural commodities
- Manage basis risk in addition to flat price risk
- Increased transportation costs and higher flat price levels = greater basis risk
- Improved capital efficiency through daily mark to market margin process
- Allow small and mid-size commercial firms to better compete
- Provides benefits of centralized clearing for products that are too small to support efficient exchange-traded futures

**The 4(d) request made by ICE Clear parallels the terms of the Orders previously issued by the Commission to the CME and other exchanges concerning the commingling of funds, and the same benefits would inure to ICE Clear market users.**

The CME continues with this theme by reminding the Commission not to overlook the question of whether a 4(d) Order permitting the funds used to margin cleared-only OTC contracts to be held in segregation would subject those funds to the bankruptcy protections set forth in Part 190 of the Commission's regulations—a matter which the Commission has addressed numerous times in the context of every Section 4(d) order issued by it.

□ On the subject of ICE Futures floor brokers and floor traders being eligible swaps participants for purposes of the subject transactions, the CME, in its submission to have its floor brokers and floor traders be eligible contract participants entitled to enter into cleared OTC transactions, stated that:

Inclusion of floor traders and floor brokers is intended to serve the public interest generally by enhancing liquidity and opportunity. CME floor brokers and floor

traders who utilize the SUB process to create positions in either 'traded and cleared' or 'cleared-only' Exchange markets will be leveraging their trading skills, experience and market expertise in such a manner as to attract additional activity and open interest onto the Exchange. In the process, they will likewise be expanding the pool of potential counterparties for OTC market participants and generally facilitating liquidity in the OTC marketplace as well. Accordingly, this strengthens the ties between, and enhances the utility of both, the exchange-traded and OTC derivatives marketplaces.

**The same holds true with respect to ICE Futures floor brokers and traders transacting in the eligible OTC contracts that will be cleared by ICE Clear.**

\* \* \*

Although the CFMA did not specifically provide for clearing of swaps involving agricultural products, the Commission has broad exemptive authority under Section 4(c) of the Act to grant the relief requested. We believe that doing so is appropriate in the circumstances presented.

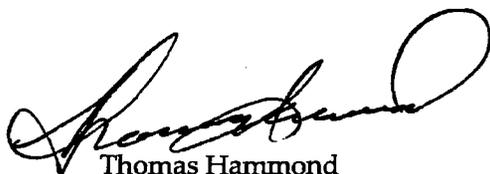
Section 4(c)(1) of the Act empowers the CFTC to "promote responsible economic or financial innovation and fair competition" by exempting any transaction or class of transactions from any of the provisions of the Act (subject to exceptions not relevant here) where the Commission determines that the exemption would be consistent with the public interest. In enacting Section 4(c), Congress noted that the goal of the provision "is to give the Commission a means of providing certainty and stability to existing and emerging markets so that financial innovation and market development can proceed in an effective and competitive manner". The Commission should recognize the growth and maturity of the agricultural markets involved in the ICE Clear and ICE Futures proposal. Coffee, sugar and cocoa are international commodities that are produced outside of the U.S. and listed for trading on markets throughout the world. The ability of the US markets to compete with respect to these products would be enhanced by granting the requested petitions.

Section 4(c)(2) provides that the Commission may grant exemptions only when it determines that the requirements for which an exemption is being provided should not apply to the agreements, contracts or transactions at issue, and the exemption is consistent with the public interest and the purpose of the Act; that the agreements, contracts or transactions will be entered into solely between appropriate persons; and that the exemption will not have a material adverse effect on the ability of the Commission or any contract market to discharge its regulatory or self-regulatory responsibilities under the Act. Issuance of the Orders sought hereunder will be in the public interest by promoting liquidity and transparency in the markets for OTC

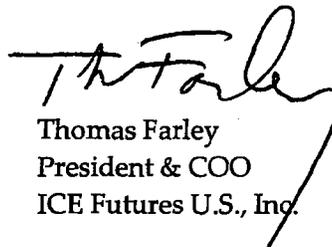
derivatives on agricultural commodities as well as futures on such commodities. Moreover, they will be entered into solely between appropriate persons because the transactions would be limited to being conducted among eligible swaps participants—a class of trader that has already been recognized by the Commission to be “appropriate persons” for these types of transactions in other contexts. There is no reason to believe that allowing the clearance of swaps in agricultural commodities would have a material, adverse affect on the ability of ICE Clear or the Commission to carry out their self-regulatory and oversight responsibilities, respectively.

In closing, we believe that all of the conditions for the exercise of the Commission’s exemptive authority under Section 4(c) are met by the proposal, and it would be appropriate for the Commission to exercise that authority to grant the requests.

Respectfully Submitted,



Thomas Hammond  
President  
ICE Clear U.S., Inc.



Thomas Farley  
President & COO  
ICE Futures U.S., Inc.

Cc: Acting Chairman Lukken  
Commissioner Chilton  
Commissioner Durn  
Commissioner Sommers  
Ananda Radhakrishnan  
Richard Shilts  
David VanWagner