



## U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Market Oversight

CFTC Letter No. 13-08  
No-Action  
April 5, 2013  
Division of Market Oversight

### **Staff No-Action Relief from the Reporting Requirements of § 32.3(b)(1) of the Commission's Regulations, and Certain Recordkeeping Requirements of § 32.3(b), for End Users Eligible for the Trade Option Exemption**

On April 27, 2012, the Commission published final commodity option rules and interim final rules ("IFR") incorporating a trade option exemption ("TOE"), subject to conditions, from most provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"),<sup>1</sup> the Commodity Exchange Act ("CEA"),<sup>2</sup> and the Commission's regulations ("Commodity Options Release").<sup>3</sup> The Commission requested comment in the Commodity Options Release on a number of questions in connection with the TOE.<sup>4</sup> In the Commodity Options Release, the Commission reiterated that commodity options are "statutorily defined as swaps" and thus "subject to the same rules applicable to any other swap."<sup>5</sup> However, the Commission added that "if the offeror, the offeree, and the characteristics of the option transaction meet the requirements of the trade option exemption, such option transactions will be exempt from the general Dodd-Frank regime, subject to specified ongoing conditions and compliance requirements discussed below, as applicable."<sup>6</sup> The Commission also advised interested parties that:

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<sup>1</sup> Public Law 111-203, 124 Stat. 1376 (2010).

<sup>2</sup> 7 U.S.C. § 1 *et seq.*

<sup>3</sup> *See* Commodity Options, 77 FR 25320 (Apr. 27, 2012). The Commission's regulations are set forth in Chapter I of Title 17 of the Code of Federal Regulations. The TOE refers to 17 CFR § 32.3.

<sup>4</sup> The TOE comment period ended on June 26, 2012. The Commission has been reviewing the comments received in response to the TOE IFR request for comment. Additionally, the Commission issued related information collection notices. *See* Agency Information Collection Activities: Proposed Collection, Comment Request: Form TO, Annual Notice Filing for Counterparties to Unreported Trade Options, 77 FR 74647 (Dec. 17, 2012); Agency Information Collection Activities under OMB Review, 78 FR 11856 (Feb. 20, 2013). The Form TO comment periods closed on February 15, 2013 and March 22, 2013, respectively. The Commission has been reviewing the comments received in response to the information collection notices regarding Form TO, including as they relate generally to the TOE reporting requirements.

<sup>5</sup> Commodity Options Release, 77 FR at 25321, 25325.

<sup>6</sup> *Id.* at 25326.

[t]he final rule and interpretations that result from the Product Definitions [proposed rulemaking] will address the determination of whether a commodity option or a transaction with optionality is subject to the swap definition in the first instance. If a commodity option or a transaction with optionality is excluded from the scope of the swap definition, as further defined by the Commission and the SEC, the final rule and/or interim final rule adopted herein are not applicable.<sup>7</sup>

On July 10, 2012, the Commission approved joint (with the SEC) final rules and interpretations further defining, among other terms, the term “swap” (“Final Swap Release”).<sup>8</sup> In the preamble of the Final Swap Release, the Commission issued a request for comment stating that market participants may rely upon its interpretation regarding forwards with volumetric options,<sup>9</sup> but also “request[ing] public comment on all aspects of its interpretation regarding forwards with embedded volumetric options . . . .”<sup>10</sup>

The Division of Market Oversight (“DMO”) previously issued a letter (the “August Letter”) providing time-limited no-action relief relating to the TOE.<sup>11</sup> The August Letter stated that DMO would not recommend that the Commission commence an enforcement action against a market participant for failure to comply with any provision of Dodd-Frank, the CEA, or the Commission’s regulations applicable to commodity options that are swaps if such market participant was in compliance with certain specified provisions of the TOE.

While the August Letter expired on December 31, 2012,<sup>12</sup> subsequently-issued staff no-action relief from certain swap reporting requirements has been effective for commodity options that otherwise would be subject to the TOE. However, the previously-issued relief from Part 45 reporting requirements for any market participant that is not a Swap Dealer (“SD”) or Major

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<sup>7</sup> Id. at 25321 n.6.

<sup>8</sup> See Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping; Final Rule, 77 FR 48207 (August 13, 2012).

<sup>9</sup> The Commission stated in the Final Swap Release that “agreements, contracts, and transactions with embedded volumetric optionality may satisfy the forward exclusions from the swap and future delivery definitions under certain circumstances.” Id. at 48238. If they do not, they may be options, and therefore swaps. If, however, such options satisfy the terms of the TOE, the persons described therein would be subject to the reduced compliance burden applicable under the TOE, and could be eligible for the no-action relief provided in this letter.

<sup>10</sup> Id. at 48241. The volumetric optionality comment period ended on October 12, 2012. The Commission has been considering the comments received in response to the volumetric optionality request for comment. Market participants may continue to rely upon the Commission’s volumetric optionality interpretation set forth in the Final Swap Release. See id. at 48238.

<sup>11</sup> CFTC No-Action Letter No. 12-06 (Aug. 14, 2012), available at <http://www.cftc.gov/ucm/groups/public/@llettergeneral/documents/letter/12-06.pdf>.

<sup>12</sup> The August Letter, by its terms, was to be “in effect through and including the earlier of (1) December 31, 2012 or (2) the effective date of any final action taken by the Commission as a result of comments received in response to the TOE IFR. In this context, ‘final action’ means a final rule, an interpretation or an order.”

Swap Participant (“MSP”) (collectively, a “Non-SD/MSP”) is set to expire on April 10, 2013.<sup>13</sup> Therefore, Non-SDs/MSPs relying on the TOE, as applicable under the terms of the TOE, are required to comply with Part 45 reporting requirements under certain circumstances as of this expiration date.<sup>14</sup> Noting this deadline, various trade option end-users recently requested no-action relief with respect to Part 45 reporting requirements for certain trade options,<sup>15</sup> citing technical and logistical impediments preventing timely compliance. Separately, other trade option end-users have requested that the Commission clarify the scope of recordkeeping requirements under § 32.3(b).

After reviewing the requests for no-action relief and clarification, as well as the comments filed with respect to the TOE IFR, DMO believes that the following relief from certain reporting and recordkeeping provisions of the TOE IFR is warranted.

#### A. No-Action Relief for Non-SD/MSPs from Certain TOE Reporting Requirements

DMO will not recommend that the Commission commence an enforcement action against a Non-SD/MSP for violating § 32.2(b)<sup>16</sup> by offering to enter into, entering into, confirming the execution of, maintaining a position in, or otherwise conducting activity related to, any transaction in interstate commerce that is a commodity option transaction, notwithstanding that, in connection with such commodity option transaction, such Non-SD/MSP is not in compliance with Part 45 reporting requirements as set forth in § 32.3(b)(1).<sup>17</sup> This no-action position is contingent upon such Non-SD/MSP and the commodity option transaction itself complying with

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<sup>13</sup> See CFTC No-Action Letter No. 12-41 (Dec. 5, 2012), available at <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/12-41.pdf>.

<sup>14</sup> See § 32.3(b)(1).

<sup>15</sup> See Letter from the Commercial Energy Working Group (March 1, 2013); Letter from the American Gas Association (March 11, 2013). Specifically, these letters requested that the Commission either (1) promulgate a TOE final rule that permits all Non-SD/MSP counterparties to report trade options exclusively pursuant to Form TO, or, alternatively, (2) extend the compliance date for reporting trade options pursuant to Part 45 as set forth in § 32.3(b)(1) until April 10, 2014.

<sup>16</sup> § 32.2 provides, in relevant part, that:

Subject to §§ 32.1, 32.4, and 32.5, which shall in any event apply to all commodity option transactions, it shall be unlawful for any person or group of persons to offer to enter into, enter into, confirm the execution of, maintain a position in, or otherwise conduct activity related to any transaction in interstate commerce that is a commodity option transaction, unless:

...

(b) Such transaction is conducted pursuant to § 32.3.

<sup>17</sup> This no-action position does not apply with respect to a trade option where an SD or MSP is a counterparty and otherwise must report the trade option pursuant to Part 45 as set forth in §§ 32.3(b)(1) and 32.3(c)(4).

all other elements of the TOE (subject to any other applicable no-action relief in effect),<sup>18</sup> as well as the following additional conditions:

- 1) the Non-SD/MSP reporting the commodity option transaction on Form TO pursuant to § 32.3(b)(2);<sup>19</sup> and
- 2) the Non-SD/MSP notifying DMO through an email to TOreportingrelief@cftc.gov no later than 30 days after entering into trade options having an aggregate notional value in excess of \$1 billion during any calendar year.<sup>20</sup>

#### B. No-Action Relief for Non-SD/MSPs from Certain TOE Recordkeeping Requirements

Section 32.3(b) provides that “[i]n connection with any commodity option transaction [eligible for the TOE], every counterparty shall comply with the swap data recordkeeping requirements of part 45 of this chapter, as otherwise applicable to any swap transaction . . . .” In discussing the TOE conditions, however, the Commission noted that “[t]hese conditions include a recordkeeping requirement for any trade option activity, *i.e.*, the recordkeeping requirements of 17 CFR 45.2,” and did not reference or discuss any other provision of Part 45 that contains recordkeeping requirements.<sup>21</sup> Therefore, DMO will not recommend that the Commission

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<sup>18</sup> DMO stresses that, among other TOE provisions, Non-SD/MSPs that rely on this no-action position with respect to certain TOE reporting requirements are still subject to Part 45 recordkeeping requirements as set forth in § 32.3(b) (subject to any other applicable no-action relief in effect). This requires, among other things, that (1) Non-SD/MSPs “keep full, complete, and systematic records, together with all pertinent data and memoranda, with respect to each [trade option] in which they are a counterparty . . . ,” and (2) all records required to be kept under Part 45 “shall be open to inspection upon request by any representative of the Commission.” See §§ 45.2(b), 45.2(h).

<sup>19</sup> This condition requires compliance with § 32.3(b)(2) irrespective of whether the commodity option transaction involves a counterparty described in § 32.3(b)(1). In other words, even if one or both Non-SD/MSP counterparties to the trade option in question have become subject to Part 45 as the reporting counterparty for swaps other than the trade option itself during the twelve months prior to entering into the trade option, in order to comply with the terms of this no-action position, each Non-SD/MSP counterparty would have to “file with the Commission by March 1 of the following year an ‘Annual Notice Filing for Counterparties to Unreported Trade Options’ on Form TO, as set forth in Appendix A to [Part 32], to be completed and submitted in accordance with the instructions thereto and as further directed by the Commission.” See § 32.3(b)(2).

<sup>20</sup> The notification required by this condition is in addition to annual reporting pursuant to Form TO as required by the first condition. For purposes of this condition, the aggregate notional value of trade options entered into should be calculated by multiplying (1) the maximum volume of the commodities that could be bought or sold pursuant to the trade options entered into by (2) the fair market value (“FMV”) of each such maximum volume. If the FMV is not a fixed number in the trade option agreement and, instead, is to be determined pursuant to a reference price source that is not determinable at the time of the trade option’s execution, the foregoing calculation should be based on the value of the reference price source at the time of execution. For example, if the FMV of oil that could be bought or sold pursuant to a trade option is to be determined pursuant to the price of a New York Mercantile Exchange oil futures contract that settles three months after the trade option is executed, the FMV should be determined using the market price of the oil futures contract at the time the trade option is executed (or as close to execution as is possible, acting in a commercially reasonable manner to contemporaneously determine such market price). Cf. Division of Swap Dealer and Intermediary Oversight Responds to FAQs About Swap Entities (discussing, among other things, the calculation of notional amounts for physical commodity swaps), available at [http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/swapentities\\_faq\\_final.pdf](http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/swapentities_faq_final.pdf).

<sup>21</sup> See Commodity Options Release, 77 FR at 25327.

commence an enforcement action against a Non-SD/MSP for violating § 32.2(b) by offering to enter into, entering into, confirming the execution of, maintaining a position in, or otherwise conducting activity related to, any transaction in interstate commerce that is a commodity option transaction, notwithstanding that, in connection with such commodity option transaction, such Non-SD/MSP complies with only the recordkeeping requirements set forth in § 45.2 of the Commission's Regulations for purposes of satisfying the § 32.3(b) recordkeeping requirement. This no-action position is contingent upon such Non-SD/MSP and the commodity option transaction itself complying with all other elements of the TOE (subject to any other applicable no-action relief in effect), as well as the following additional conditions:

- 1) if the Non-SD/MSP's counterparty to the trade option at issue is an SD or MSP, the Non-SD/MSP obtaining a legal entity identifier ("LEI") pursuant to § 45.6 and providing such LEI to the SD or MSP counterparty;<sup>22</sup> and
- 2) the Non-SD/MSP notifying DMO through an email to TOreportingrelief@cftc.gov no later than 30 days after entering into trade options having an aggregate notional value in excess of \$1 billion during any calendar year.<sup>23</sup>

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The no-action relief provided herein contains a collection of information, as that term is defined in the Paperwork Reduction Act.<sup>24</sup> Therefore, a control number for the collection must be obtained from the Office of Management and Budget. In accordance with 44 U.S.C. § 3507(d) and 5 C.F.R. §§ 1320.8 and 1320.10, DMO will, by separate action, prepare an information collection request for review and approval by OMB.

The no-action positions contained herein are effective as of April 5, 2013, represent the views of DMO only, and do not bind the Commission or any other Division or Office of the Commission's staff. Further, this letter (and the relief contained herein) is based upon the representations made to DMO. Any different, changed, or omitted material facts or circumstances might render this letter void. As with all no-action letters, DMO retains the authority to condition further, modify, suspend, terminate, or otherwise restrict the terms of the no-action relief provided herein, in its discretion.

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<sup>22</sup> An SD or MSP that otherwise would report the trade option at issue pursuant to § 32.3(b)(1) is required to identify its counterparty to the trade option by that counterparty's LEI in all recordkeeping as well as all swap data reporting. See, e.g., §§ 23.201, 23.204, 45.6.

<sup>23</sup> See supra note 20.

<sup>24</sup> 44 U.S.C. §§ 3501 et. seq.

If you have any questions regarding the content of this staff no-action letter, please contact Don Heitman at [dheitman@cftc.gov](mailto:dheitman@cftc.gov) or (202) 418-5041, David Aron at [daron@cftc.gov](mailto:daron@cftc.gov) or (202) 418-6621, or Graham McCall at [gmccall@cftc.gov](mailto:gmccall@cftc.gov) or (202) 418-6150.

Sincerely,

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