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COMMODITY FUTURES TRADING COMMISSION
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DIVISION OF
ECONOMIC ANALYSIS

September 2, 1992

Dear

This is in response to your letter of July 27, 1992, in which you requested that the Division of Economic Analysis (the "Division") confirm that it will not recommend any enforcement action be initiated against for violation of Federal speculative position limits for positions taken by as part of spread or arbitrage trading in the GSCI Nearby Index futures contracts and options on such futures contracts (collectively, the "GSCI contracts") and in the underlying futures contracts or options on such futures contracts ("underlying contracts"). The facts which you have represented in your letter are as follows.

The GSCI Nearby Index futures contract is based on the Goldman Sachs Commodity Index, a world production-weighted, arithmetic average of the prices of futures contracts on physical commodities which satisfy specified eligibility criteria. The components of the GSCI presently include, among other futures contracts, those based on wheat, corn, soybeans and cotton which are subject to Commission position limits.

represents that it intends to trade the GSCI contract for its proprietary account in two ways: (1) by voluntarily acting as a market-maker, providing liquidity to the market during its "start-up phase"; and (2) by engaging in arbitrage transactions between the GSCI contracts and the underlying futures contracts. expects to conduct this trading activity primarily through the use of spread transactions comprised of positions in the GSCI contracts and offsetting positions in the futures or option contracts underlying the GSCI, in order to reduce the risk which would otherwise be incurred through the trading of the GSCI contracts alone. For example, if sold a GSCI contract, it would purchase each of the underlying futures contracts, in quantities which reflect the weighing of each such contract in the GSCI. Because movements in the "basket" of futures contracts included in the GSCI will necessarily be reflected in movements in the value of the GSCI itself, any losses on the GSCI contract position should be offset by gains on the positions in the underlying contracts. Conversely, if purchased the GSCI contract, it would sell the underlying futures contracts, based on the same weighing formula.

Each such spread or arbitrage position in the underlying futures contracts would, to the extent possible, be in the same delivery month as the month which is reflected in the corresponding GSCI contract. anticipates that the GSCI contract positions and the positions in the underlying contracts would be established simultaneously or nearly simultaneously, in order to achieve risk reduction objectives.

intends to liquidate each such position in a GSCI contract, along with its position in the corresponding underlying contracts, by no later than the expiration day of the GSCI contract, which will be the fourth business day of the delivery month. Accordingly, will not hold such spread positions in the spot month of any of the underlying futures contracts. In addition, anticipates that it will liquidate its spread position during the course of its trading on the expiration day of the GSCI contract. As a result, does not expect such liquidations to occur at the close of the market, although it could be necessary to liquidate positions at the close under certain market conditions.

Commission Rule 150.3(a) provides exemptive relief from Commission speculative limits for certain kinds of spread and arbitrage trading. Commission Rule 150.3(a)(2) provides an exemption for spread or arbitrage positions between futures and option contracts traded on the same board of trade in any one commodity, for positions outside of the spot month, which are as a totality offsetting. Commission Rule 150.3(a)(3) provides an exemption for spread or arbitrage positions between single months of a futures contract traded on the same board of trade outside of the spot month.

Since the spread or arbitrage trading described in your letter does not involve the same commodity, and does not involve commodities traded on the same board of trade, it does not currently qualify for exemptive relief under Commission Rule 150.3. Nevertheless, you represent that the positions taken in the GSCI contracts and the underlying futures contracts will be as a totality offsetting; because the GSCI contracts are based on the weighted values of the underlying futures contracts, the legs of the spread or arbitrage positions will be precisely opposite and offsetting and movements in the underlying contracts will necessarily be reflected in the value of the GSCI contracts.

The Division of Economic Analysis is of the opinion that the spread and arbitrage trading described in your letter is analogous to the spread and arbitrage trading provided exemptive relief under Commission rule 150.3. Accordingly, in light of the representations made in your letter, the Division will not recommend to the

Commission any enforcement action under §4a(1) of the Commodity Exchange Act (7 U.S.C. §6a(1)) related to spread and arbitrage trading of the GSCI contract and the underlying contracts, as described in your letter, if the following conditions are met: (1) the spread or arbitrage positions are as a totality offsetting; (2) the positions in the underlying contracts are not in the spot month; and (3) the positions in any individual month or in all months combined do not exceed the all months combined limit specified in Commission Rule 150.2

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This determination does not excuse from complying with any otherwise applicable provisions of the Commodity Exchange Act or the Commission's regulations, thereunder. This determination is based upon the facts and representations contained in your letter and conversations with the staff. Any different, omitted or changed facts or conditions might require a different conclusion. Moreover, it should be noted that this determination is that of the staff of the Division of Economic Analysis and is not binding upon the Commission or on any other of its staff. Finally, any subsequent rule amendments relating to the application of speculative position limits may require a reconsideration of this determination.

Sincerely yours,

Gerald D. Gay
Director