New York
Mercantile Exchange

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September 26, 2005

Ms. Jean A. Webb
Secretary to the Commission
Commodity Futures Trading Commission
One Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

COMMENT

Re: Technical and Clarifying Amendments to Rules for Exempt Markets, Derivatives Transaction Execution Facilities and Designated Contract Markets, and Procedural Changes for Derivatives Clearing Organization Registration Applications (hereafter, the "Clarifying Amendments"). 70 *Fed. Reg.* 39672 (July 11, 2005).

Dear Ms. Webb:

The New York Mercantile Exchange, Inc. ("NYMEX" or the "Exchange"), [1] appreciates the opportunity to comment on behalf of itself and its wholly-owned subsidiary, Commodity Exchange, Inc. ("COMEX"), to the Commodity Futures Trading Commission ("CFTC" or "Commission") on the proposed Clarifying Amendments. NYMEX supports the Commission on its efforts to review and clarify various possible ambiguities that arose as a result of its adoption of various amendments to its Regulations implementing the Commodity Futures Modernization Act ("CFMA"). However, as discussed below, the Exchange suggests that the Commission consider exercising restraint in this regard. It would be unfortunate if this laudable undertaking of the CFTC had the unintended consequence of curtailing the exchanges' ability to exercise reasonable discretion in establishing the manner in which it complies with the CFMA's Core Principles.

Of primary concern to the Exchange is the Commission's proposed amendment to Regulation 38.2 to "make clear that the references therein to reserved provisions of the regulations applicable to [Designated Contract Markets] also include related definitions

[1] NYMEX is a for-profit corporation organized under the laws of the State of Delaware. It is a designated contract market for the trading of numerous commodity futures and commodity futures option contracts. NYMEX is the largest exchange in the world for the trading of futures and option contracts based on physical commodities. In 2004, more than 169 million contracts were traded at the Exchange. Public investors in our markets include institutional and commercial producers, processors, marketers and users of energy and metals products.

New York Mercantile Exchange, Inc.
World Financial Center
One North End Avenue
New York, NY 10282-1101
(212) 299-2000

The New York Mercantile Exchange, Inc., is composed of two divisions. The NYMEX Division offers trading in crude oil, heating oil, unleaded gasoline, natural gas, electricity, coal, propane, platinum, and palladium. The COMEX Division offers trading in gold, silver, copper, and aluminum.

and cross-referenced sections cited in those reserved provisions." In furthering the goals of the CFMA, effective October 9, 2001, the Commission used its broad exemptive authority under Section 4(c) of the Commodity Exchange Act ("CEA") to, *inter alia*, promulgate §38.2 of the Commission's Regulations, exempting a Designated Contract Market ("DCM") from all then existing Commission regulations governing the activities of such entities, other than certain specifically reserved sections. The Commission was very judicious in selecting those provisions to reserve, and the Exchange believes that adding a general provision at this time to include under that umbrella all cross-referenced sections and related definitions could have the unintended effect of bringing back into force overly prescriptive regulations of the kind the CFMA was appropriately intended to eliminate.

As an example, §1.63(c), was specifically reserved under §38.2, and renders a member ineligible for disciplinary or governing board service if any of a number of conditions listed in §1.63(b) was satisfied. Although §1.63(b) was not specifically reserved, the Exchange concedes that this provision should be re-incorporated because §1.63(c) would essentially be meaningless without cross-referencing it. One of the conditions listed in that subsection included the member having been subject to a disciplinary action by the DCM for having committed a "disciplinary offense" within the prior three years. The definition of a "disciplinary offense," however, is contained in §1.63(a), which also was not specifically reserved, but includes, *inter alia*, reporting or recordkeeping infractions by a member for which a total of $5000 in fines had been assessed within a calendar year. This is an extremely specific provision and, since promulgation of §38.2, the Exchange staff has reasonably taken the view that it was too overly specific and prescriptive in nature to have been intended as reserved. In fact, the Exchange has since made certain rule and policy amendments consistent with that view.

On January 28, 2002, NYMEX submitted to the Commission, by self-certification under CEA §5c(c)(1) and Commission Regulation 40.6(a) an amendment to NYMEX Rule 3.03 that removed from the list of disciplinary offenses that disqualified Exchange members from Board of Directors or disciplinary committee service reporting or recordkeeping violations resulting in fines totaling $5000 within a calendar year. During the course of subsequent discussions with Commission staff, Exchange staff explained that the Exchange would instead implement a procedure by which disciplinary committees reviewing settlements of cases concerning such offenses would consider, on a case by case basis, whether the circumstance surrounding the reporting or recordkeeping offenses in question should warrant disqualification. In connection with further discussions with Commission staff, on July 12, 2005, the Exchange self-certified additional amendments to Rule 3.03 codifying the procedure by which reporting and recordkeeping violations resulting in cumulative fines of over $5000 in a calendar year would be considered with regard to Board and disciplinary committee service. Section 5(d) of the CEA sets forth the Core Principles for Contract Markets and gives boards of trade "reasonable discretion in establishing the manner in which it complies" with them. The Exchange did then, and does still believe that the procedure described above satisfies Core Principle 14, which requires a DCM to ensure appropriate fitness standards for members of its governing board and disciplinary committees.

The reintroduction of §1.63(a) in its current form, which includes specific definitions of what constitutes a disciplinary offense on a DCM, and specifies a dollar amount and timeframe – five thousand dollars within a calendar year – for recordkeeping fines that will trigger a bar on governing board service, would deprive DCMs of the flexibility they were given under the CFMA to determine how best to self-regulate. This flexibility is necessary now more than ever given the disparate business models the various exchanges are adopting. Currently, NYMEX's Board of Directors has greater representation from the floor community than some other DCMs. Therefore, prohibitions on service connected with technical floor violations (primarily those relating to late submission of pit cards) unequally impacts NYMEX. Further, since DCMs continue to have discretion to determine how severely to sanction members for individual recordkeeping infractions, inclusion of a specific cumulative one-size-fits-all fine level in the Commission's Regulations at which to trigger a bar on Board or Committee service is inappropriate, and could have a chilling effect on DCMs setting sanction levels high enough to promote compliance for fear of unnecessarily triggering consequences that could disrupt its governance.

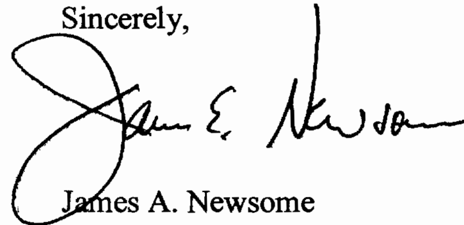
NYMEX acknowledges that, for the most part, reincorporation of cross-referenced sections and related definitions may be necessary. However, the Exchange suggests that hastily reinstating ***all*** such sections would go beyond clarifying the intent behind the Commission's rulemakings implementing the CFMA, and in some cases would be a step backward and contrary to the spirit of the CFMA. The provision discussed above is of a nature that obviously conflicts with the Commission's intent in initially granting the general exemption in §38.2. The Exchange respectfully requests that the Commission staff instead carefully review such sections and that the Commission selectively add to the list of reserved sections in §38.2 those specific provisions determined to be appropriate and of continuing value. The Exchange also respectfully urges the Commission, in re-implementing such provisions, to only apply them prospectively. In the case of §1.63(a) discussed above, reestablishing a specific fine limit at which to trigger a bar on committee service, and applying that limit retroactively could unjustly subject Exchange members to penalties beyond those upon which they agreed in submitting offers of settlement. In such cases, the knowledge that a final action would amount to a "barrable offense" could have impacted a member's decision on whether and how to settle the charged violations. Such decisions were made in the context of NYMEX rule changes that have now been in effect for more than three and one half years. As members who would become subject to the prohibition as a result of re-implementing §1.63(a) would have had no meaningful opportunity to defend themselves against this consequence, retroactive application of that section would be unfair and inappropriate.

The Exchange also at this time respectfully suggests that the Commission amend the definition of "Emergency" in §40.1 of the Commissions Regulations. This was not among the proposed Clarifying Amendments, but the Exchange believes such an amendment would nevertheless be appropriate. The current regulation defines an Emergency as a condition that "in the opinion of the governing board of [a DCM] requires immediate action and threatens or may threaten such things as the fair and

orderly trading in" its markets. The Exchange staff notes that under such a condition, the governing board may not be in a position to issue such an opinion in a timely manner to address the condition. As a matter of interpretation, the Exchange believes that the opinion of a subcommittee or exchange official that is duly authorized under a DCM's rules to act with the governing board's authority in such circumstances satisfies this requirement, such that the DCM could take such actions as necessary and appropriate under Part 40 of the Commission's Regulations. Nevertheless, the Exchange staff would recommend that the language in §40.1 be amended to make this clear.

NYMEX thanks the Commission for the opportunity to submit comments concerning the proposed Clarifying Amendments, and would be pleased to furnish additional information in this regard. If you have any questions, please do not hesitate to contact the undersigned.

Sincerely,



James A. Newsome
President