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CME Group
A CME/Chicago Board of Trade/NYMEX Company

Craig S. Donohue
Chief Executive Officer

July 13, 2009

VIA ELECTRONIC MAIL

David Stawick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581
secretary@cftc.gov

COMMENT

Re: ICE Henry Financial LD1 Fixed Price Contract - 74 Fed. Reg. 28029 (June 12, 2009)

Dear Mr. Stawick:

CME Group Inc. ("CME Group"), on behalf of its four designated contract markets ("DCMs"), appreciates the opportunity to comment on the Commodity Futures Trading Commission's (the "CFTC" or "Commission") notice of intent published in the Federal Register ("Release"), pursuant to its authority under Section 2(h)(7) of the Commodity Exchange Act ("CEA" or "Act") and Commission Rule 36.3(c)(3), to undertake a determination whether the Henry Financial LD1 Fixed Price Contract ("Henry Hub contract") traded on the Intercontinental Exchange, Inc. ("ICE"), which is operating as an exempt commercial market ("ECM"), performs a significant price discovery function and thus should be determined to be a Significant Price Discovery Contract ("SPDC").

CME Group was formed by the merger of Chicago Mercantile Exchange Holdings Inc. and CBOT Holdings Inc. in 2007, and subsequently merged with NYMEX Holdings, Inc. in 2008. CME Group is the parent of four DCMs: (1) Chicago Mercantile Exchange, Inc ("CME"); (2) the Board of Trade of the City of Chicago, Inc. ("CBOT"); (3) the New York Mercantile Exchange, Inc. ("NYMEX"); and (4) the Commodity Exchange, Inc. ("COMEX"). CME is also among the largest derivatives clearing organizations in the world, and CME Clearing includes CME ClearPort®, a set of flexible clearing services open to over-the-counter market participants to substantially mitigate counterparty risk and provide capital efficiencies across asset classes. The CME Group exchanges serve the risk management needs of customers around the globe.

As an international marketplace, the CME Group exchanges bring buyers and sellers together on the CME Globex electronic trading platform and on trading floors in Chicago and New York. The CME Group exchanges offer the widest range of benchmark products available across all major asset classes, including futures and options based on interest rates, equity indexes, foreign exchange, energy, emissions, agricultural commodities, metals, and alternative investment products such as weather and real estate.

Overview

In the Release, the Commission indicated that it would be especially useful for commenters to address the factors (set forth in Appendix A to Part 36 of the CFTC's rules) used to analyze whether a contract serves a significant price discovery function. Appendix A(1) sets forth the four factors prescribed by the statute: "Price Linkage; Arbitrage; Material Price Reference; and Material Liquidity." As further discussed below, the CME Group believes that ICE's Henry Hub contract clearly satisfies all four factors used in determining a SPDC.

Background

In Appendix A(2) to Part 36, the Commission clarified that: "[n]ot all listed factors must be present to support a determination that a contract performs a significant price discovery function." The CFTC further noted in Appendix A(2) that the statute did not prioritize the factors and also did not specify the degree to which a significant price discovery contract must conform to the various factors. In addition, the Commission expressed its belief that the Arbitrage and Material Price Reference factors could be considered separately from each other. In other words, the CFTC could determine that a contract served a significant price discovery function based on the presence of one of these factors and the absence of the other.

The Release also requested that commenters identify the capacity in which they are knowledgeable about the Henry Hub contract. As to knowledge concerning ICE's Henry Hub contract, we believe that it is relevant to note that the NYMEX lists for trading its Natural Gas (hereafter referenced by NYMEX commodity code "NG") futures contract, which is physically settled and which competes directly with ICE's Henry Hub contract, which is financially settled. NYMEX's NG futures contract has a contract size of 10,000 million British thermal units (mmBtu), while the Henry Hub contract is priced in relation to a contract size of 2,500 mmBtus.

In addition, NYMEX also lists for trading two other futures contracts that are both financially settled and that also compete with ICE's Henry Hub contract: (1) the Henry Hub Natural Gas Swap futures contract ("NN"); and (2) the Henry Hub Natural Gas Penultimate Swap futures contract ("NP"). These contracts both have a contract size of 2,500 mmBtus. As suggested by its name, the last trading day of the NP futures contract is one business day prior to the last trading day for the NG and NN futures contracts. Like the subject ICE Henry Hub contract, the NN and NP futures contracts are both settled on the basis of the NG settlement prices.

As part of the CFTC's "Report on the Oversight of Trading on Regulated Futures Exchanges and Exempt Commercial Markets" ("ECM Study") which was issued by the CFTC in October 2007, the CFTC's Office of Chief Economist examined the price interaction between NYMEX's NG and ICE'S Henry Hub contract. Specifically, as detailed in the Release itself:

> "the ECM Study referenced an analysis of whether the NYMEX, ICE, or both facilities exhibit price leadership with respect to their natural gas contracts. If a particular exchange's prices lead those on another exchange, then the former exchange's contract is thought of as a price discovery market. In 2006, the ICE's natural gas contract exhibited price leadership on 20 percent of the contract days; the NYMEX's physically-delivered natural gas contract, on the other hand, exhibited price leadership on 63 percent of the contract days. Based on these factors, the ECM Study concluded that the ICE and the NYMEX contracts are both price discovery venues for natural gas trading." (Release at p. 28030.)

These results are consistent with the findings of a report, issued several months prior to the ECM Study by the Senate Permanent Subcommittee on Investigations, which was generated in response to the trading of Amaranth LLC, a large energy hedge fund, in both the NYMEX and ICE trading venues. In that report, which was entitled "Excessive Speculation in the Natural Gas Market" and which was released on June 25, 2007 ("Subcommittee Report"), the Subcommittee made a series of findings, which included the following:

> "Significant volumes of natural gas are traded on both NYMEX and ICE, and both markets play a key role in setting U.S. natural gas prices. The contracts used on NYMEX and ICE to trade natural gas, called futures contracts on NYMEX and swaps on ICE, are equivalent financial products that serve the same risk management purposes. Traders routinely buy and sell natural gas contracts on both NYMEX and ICE, and hold positions in both markets. The price of NYMEX futures and ICE swaps are virtually identical up until the final half hour of the last trading day of the NYMEX contract, when NYMEX and ICE prices typically differ by a few cents at most." (Press Release, U.S. Senate Committee on Homeland Security and Government Affairs - Permanent Subcommittee on Investigations, Investigations Subcommittee Releases Levin-Coleman Report on Excessive Speculation in the Natural Gas Market, June 25, 2007.)

Both the ECM Study and the Subcommittee Report were based on price data for trading activity in 2006. Unfortunately, the CME Group is unable to provide meaningful comment to the Commission on price data in response to the Release because ICE does not make price transparency data broadly available. ICE's perspective also may highlight the significant differences that continue to exist between fully regulated DCMs, which emphasize price transparency and market integrity, and ECMs.

Material Liquidity

Although volume and open interest data by contract are not routinely made public by ICE, the Release confirmed that the subject Henry Hub contract averaged 449,010 contracts traded daily during the first quarter of 2009. Based on that figure, a grouping of competing contracts that includes the Henry Hub contract and NYMEX's NG, NN and NP contracts had an overall average daily trading volume of

1,133,075 contracts (for convenience stated in ICE equivalents) during 1Q 2009. As a reminder, all four of these contracts are settled on the basis of the settlement prices for NYMEX's NG contract.

In other words, when trading activity in the Henry Hub contract is put in the context of the relevant competing contracts at NYMEX, including both financially-settled and physically-settled contracts, ICE's Henry Hub contract nonetheless had a 40% market share of that trading activity. Accordingly, whether viewed in terms of outright volume or in terms of market share of a large and active market, we believe it is clear that ICE's Henry Hub contract easily satisfies the standards for Material Liquidity.

Price Linkage

As to Price Linkage, as noted in the Release itself, ICE's Henry Hub contract continues to have the same exact settlement price as the NYMEX NG contract. In Appendix A, the Commission specifies that, as a threshold, it "will consider a 2.5 percent price range for 95 percent of contemporaneously determined closing, settlement, or other daily prices over the most recent quarter to be sufficiently close for a linked contract potentially to be deemed a significant price discovery contract." With regard to final settlement, the product specifications for the Henry Hub contract explicitly provide for final settlement to be equal to the final settlement price of the corresponding NYMEX natural gas futures contract. Thus, there would appear to be little chance that the Henry Hub contract will deviate from the NYMEX settlement price for final settlement. With regard to trading days prior to the final day of trading, we are not aware of any instances in recent years where the settlement price for ICE's Henry Hub contract has varied from the NYMEX NG settlement price.

Arbitrage

With respect to Arbitrage, we do not have access to the price tick data for ICE's Henry Hub contract to be able to comment on recent price interactions between the NG and Henry Hub contracts. However, on an anecdotal level, we were advised by market participants in 2007 that during most of the trading cycle of a listed futures contract month, there was a range of five to twelve ticks separating the competing NYMEX and ICE products. (The NYMEX NG contract has a minimum price fluctuation or trading tick of $.001, or .01 cents per mmBtu.) NYMEX staff was advised by market participants who traded on both markets at that time that a rise (fall) in price on one trading venue would be followed almost immediately by a rise (fall) in price on the other trading venue, whether the change in price be initiated on either NYMEX or ICE.

More recently, in checking informally with market participants engaged in arbitrage activity between the two contracts, we have been advised that, while the tick spread can range from zero to 12 ticks, most recently the spread has generally been in the range of 8-9 ticks. This anecdotal information indicates that the market dynamics between these two contracts has not changed significantly since 2007. Thus, there continues to be strong and active arbitrage between the two contracts, which should satisfy this factor.

Furthermore, in Appendix A, the CFTC notes that, as part of its Arbitrage analysis, it will consider if, over the most recent quarter, greater than 95 percent of the closing or settlement prices of the contract, which

have been calculated using transaction prices, fall within 2.5 percent of the closing or settlement price of the contract or contracts to which it could be arbitraged. While ICE's settlement price for its Henry Hub contract is based upon reliance on the NYMEX settlement price rather than transaction prices on ICE itself, given the historically tight intra-day price linkage between the two competing contracts, we are confident that an analysis of transaction prices also will reach this same result.

Material Price Reference

With regard to the fourth factor, as noted above, Appendix A confirms that the CFTC could determine that a contract served a significant price discovery function based, for example, on the presence of Arbitrage and the absence of Material Price Reference. The statutory standard for Material Price Reference is "the extent to which, on a frequent and recurring basis, bids, offers or transactions in a commodity are directly based on, or are determined by referencing, the prices generated by agreements, contracts or transactions being traded or executed on the electronic trading facility."

It is true that ICE itself relies on the settlement prices generated by NYMEX for its own settlement prices in the Henry Hub contract rather than on prices generated by its own system. That stated, Appendix A further provides that the CFTC expects that

> "as a contract begins to be relied upon to set a reference price, market participants will be increasingly willing to purchase price information. To the extent, then, that an electronic trading facility begins to sell its price information regarding a contract to market participants or industry publications, the contract will meet a threshold standard to indicate that the contract potentially is a significant price discovery contract."

In that regard, it is our understanding that, for several years now, ICE has been selling its price information regarding the Henry Hub contract to interested persons.

Conclusion

In conclusion, we believe that ICE's Henry Hub contract clearly satisfies all four factors used in determining a SPDC. We are also confident that a review of recent price interaction between the NYMEX NG and ICE Henry Hub contract undertaken by the professional staff at the CFTC will provide further confirmation for this conclusion and determination.

CME Group thanks the Commission for the opportunity to comment on this matter. We would be happy

to discuss any of these issues with Commission staff. If you have any comments or questions, please feel free to contact me at (312) 930-8275 or Craig.Donohue@cmegroup.com; or Brian Regan, Managing Director and Regulatory Counsel, at (212) 299-2207 or Brian.Regan@cmegroup.com.

Sincerely,

Craig S. Donohue

Craig S. Donohue

CSD/7475 CFTC Comment Letter

cc: Chairman Gary Gensler
Commissioner Michael Dunn
Commissioner Bart Chilton
Commissioner Jill Sommers
Thelma Diaz