



U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Market Oversight

CFTC Letter No. 12-06
No-Action
August 14, 2012
Division of Market Oversight

Staff No-Action Relief: Temporary Relief for Persons Eligible for the Trade Option Exemption from the Requirements of §§ 32.3(b) and 32.3(c)(1), (3), (4) and (5) of the Commission's Regulations

On April 27, 2012, the Commission published final commodity option rules and interim final rules incorporating a trade option exemption ("TOE IFR"), subject to conditions, from most provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"),¹ the Commodity Exchange Act ("CEA")² and the Commission's regulations.³ In that April 27th release, the Commission reiterated that commodity options are "statutorily defined as swaps" and thus "subject to the same rules applicable to any other swap."⁴ 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."⁵ The Commission also advised interested parties that

[t]he final rule and interpretations that result from the Product Definitions NPRM 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.⁶

On July 10, 2012, the Commission approved joint (with the Securities and Exchange Commission ("SEC")) final rules and interpretations further defining, among other terms, the

¹ Public Law 111-203, 124 Stat. 1376 (2010).

² 7 U.S.C. § 1 et seq.

³ See Commodity Options, 77 Fed. Reg. 25320. The Commission's regulations are set forth in Chapter I of Title 17 of the Code of Federal Regulations.

⁴ *Id.* at 25321 and 25325, respectively.

⁵ *Id.* at 25326.

⁶ *Id.* at 25321, n.6.

term “swap.”⁷ In the preamble of the Federal Register release containing those rules further defining the term “swap” (“Final Swap Release”), the Commission issued a request for comment stating that, while market participants may rely upon its interpretation regarding forwards with volumetric options,⁸ “the CFTC believes that it would benefit from public comment about its interpretation, and therefore requests public comment on all aspects of its interpretation regarding forwards with embedded volumetric options”⁹ The Commission included seven specific questions regarding embedded volumetric optionality and the Commission’s related interpretation¹⁰ and stated that:

it is expected that CFTC staff will be issuing no-action relief with respect to the conditions of the modified trade option exemption (except the enforcement provisions retained in § 32.3(d)) until December 31, 2012. This extension will afford the CFTC an opportunity to review and evaluate the comments received on both the interpretation above regarding embedded volumetric optionality, and the modified trade option exemption, in order to determine whether any changes thereto are appropriate.¹¹

To effectuate the Commission’s intent that market participants not be subject to any of the conditions for relying upon the trade option exemption set forth in § 32.3 other than those set forth in § 32.3(c)(2) (position limits)¹² and § 32.3(d), the Division of Market Oversight (“DMO”) will 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 swaps¹³ if such market participant is in compliance with:

⁷ 77 FR 48208 (August 13, 2012).

⁸ 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 trade option exemption set forth in § 32.3, once § 32.3 becomes effective, the persons described therein would be subject to a reduced compliance burden.

⁹ Final Swap Release at 48241.

¹⁰ *See id.* at 48241- 48242.

¹¹ *Id.* at 48241, n.374.

¹² While the Commission did not indicate in the Final Swap Release that this no-action letter might also reserve § 32.3(c)(2), DMO believes that, in light of the Commission’s separate, ongoing efforts to modify the position limit regime (*see, e.g.*, Aggregation, Position Limits for Futures and Swaps, 77 Fed. Reg. 31767 (May 30, 2012), proposing certain modifications to the Commission’s policy for aggregation under the position limits regime in Commission regulations), it is not appropriate to include position limits in the scope of the no-action position contained in this letter.

¹³ The Commission noted in the preamble of the final Commodity Options release that it used the term, “commodity options” “to apply solely to commodity options not excluded from the definition set forth in CEA section 1a(47)(A).” 77 Fed. Reg. 25321 n.6. No relief from the regulatory regime administered by the Commission is needed with respect to options that are excluded from the Commission’s jurisdiction.

(1) the conditions set forth in § 32.3(a) with respect to commodity options described therein;¹⁴

(2) § 32.3(c)(2) (position limits); and

(3) the provisions of the CEA and the Commission's regulations set forth in § 32.3(d) (prohibitions on fraud, manipulation and other abusive practices, and related enforcement provisions),

in each case, subject to any additional no-action relief provided by the Commission with respect to such obligations.¹⁵

The no-action relief contained herein commences on the date of this letter and is 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.¹⁶ In this context, "final action" means a final rule, an interpretation or an order.

The no-action position taken herein is taken by DMO and does not bind the Commission or any other Division or Office of the Commission's staff. 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.

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

Sincerely,

Richard A. Shilts
Director
Division of Market Oversight

¹⁴ Commodity options not satisfying such conditions are not the subject of this relief and must comply with all applicable provisions of Dodd-Frank, the CEA and the Commission's regulations as of the applicable effective or compliance date.

¹⁵ In other words, the relief set forth in this no-action letter is not exclusive. Any additional no-action or other relief the Commission or its staff may provide during the pendency of this no-action relief would supersede or supplement this relief.

¹⁶ See Final Swap Release at 48241, n.374 ("This extension will afford the CFTC an opportunity to review and evaluate the comments received on both the interpretation above regarding embedded volumetric optionality, and the modified trade option exemption, in order to determine whether any changes thereto are appropriate.").