

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:FIP:B01

PLR-138605-06

Date:

March 28, 2007

Legend:

Exchange =

Parent =

Clearing House =

State =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

Date 9 =

Date 10 =

Dear :

This is in reply to a letter dated August 7, 2006, and subsequent correspondence, requesting a ruling that Exchange (formerly the) is a “qualified board or exchange” within the meaning of § 1256(g)(7)(C) of the Internal Revenue Code.

Facts:

Exchange is a private unlimited company incorporated under the Companies Acts 1948 to 1976 at Cardiff (United Kingdom) on Date 1. Exchange is an indirect, wholly-owned subsidiary of Parent, a State corporation. Exchange is a United Kingdom Recognised Investment Exchange that offers electronic trading of a variety of energy commodity derivatives contracts including commodity futures contracts and futures contract options. The electronic platform on which these contracts are traded is owned and operated by Parent. Exchange is overseen by the United Kingdom’s Financial Services Authority pursuant to the United Kingdom’s Financial Services and Markets Act 2000 (FSMA).

The three categories of futures contracts that Exchange currently offers are oil contracts, utility contracts, and emissions contracts. All Exchange contracts are cleared and settled by Clearing House, which is recognized by Her Majesty’s Treasury, on the recommendation of the Financial Services Authority, as a Recognised Clearing House under Part XVIII of the FSMA. Clearing House acts as counterparty and guarantor to each transaction executed on Exchange contracts.

Exchange’s annual accounting period is the calendar year and its overall method of accounting is the accrual method. Exchange did not file a United States federal income tax return for its taxable year ended Date 2, and is not expected to file a United States federal income tax return for its taxable year ending Date 3. Parent filed Form 5471, Information Return of U.S. Persons With Respect To Certain Foreign Corporations with respect to Exchange for its taxable year ended Date 4, and will file Form 5471 for its taxable year ended Date 2.

In a letter dated Date 5, the Commodity Futures Trading Commission (CFTC), granted no-action relief to Exchange permitting it to make its electronic trading and matching system available in the United States, notwithstanding that Exchange was not designated as a contract market pursuant to sections 5 and 5a of the Commodity

Exchange Act. The Date 5, no-action relief letter was subsequently amended by CFTC no-action letters as follows.

- (1) Amended on Date 6, to permit the U.K. natural gas futures contract to trade on the electronic platform.
- (2) Amended on Date 7, to permit and gas oil futures contracts to trade on the electronic trading platform during early morning (U.K. time) trading sessions.
- (3) Amended on Date 8, to extend early morning (U.K. time) trading sessions in futures and gas oil futures contracts.
- (4) Amended on Date 9, to make available on the electronic trading platform all contracts traded during the course of the entire trading day.

The CFTC's Division of Market Oversight issued a letter on Date 10, to Exchange reaffirming the continued validity of its Date 5, no-action letter in response to Exchange's

On November 2, 2006, the CFTC published in the Federal Register a Statement of Policy that affirmed the use of the no-action process to permit foreign boards of trade to provide direct access to their electronic trading systems to U.S. members or authorized participants without seeking designation under the Commodity Exchange Act as a contract market. In the policy statement, the CFTC endorsed the scope of the review under the no-action process, which in part, it described as follows:

The scope of review that was established by Commission staff in the DTB no-action letter and refined in subsequent no-action letters focuses on establishing the "bona fide" status of the foreign board of trade and finding that no public interest would be adversely affected by persons in the U.S. directly accessing the foreign board of trade.

In general, staff reviews information and representations provided by the applicant that relate to, among other things, the rules and structure of the applicant exchange (with an emphasis on the exchange's financial integrity,

market surveillance, trade practice and rule enforcement regime), various system integrity protections that govern the foreign board of trade's electronic trading system (using as a template the *1990 Principles for the Oversight of Screen-Based Trading Systems*), the system's related clearing and customer default protections, and information concerning the regulatory structure in the applicant's jurisdiction, with a specific emphasis on market regulation. The staff also reviews the adequacy of information sharing with the Commission by the market and its regulator. Based upon its review of the documents and representations submitted by the applicant, and subject to compliance with various conditions (e.g., representations governing access to books and records and the appointment of a U.S. agent for service of process), staff might conclude that granting no-action relief would not be contrary to the public interest.

Essentially, as it has evolved, the staff review seeks to determine that the applicant foreign board of trade is subject to governmental authorization, appropriate rules prohibiting abusive trading practices, and continuing oversight by a regulator that has powers to intervene in the market and share information with the Commission. This review generally reflects the internationally accepted approaches used by many developed market jurisdictions to govern access to foreign electronic exchanges. These approaches generally are based upon a review of, and ongoing reliance upon, the foreign market's "home" regulatory regime, and are designed to maintain regulatory protections while avoiding the imposition of duplicative regulation.

The Commission finds that the staff review appropriately addresses the Commission's concern that relief will only be granted with respect to *bona fide* foreign boards of trade. The Commission also finds that the staff's review of foreign board of trade representations and the related information submitted with respect to system integrity, clearing procedures and default protections is appropriately focused and respects the prohibitions of section 4(b). Finally, the various terms and conditions that have been imposed in the no-action letters have been reasonably and appropriately tailored to the factual circumstances raised by the applications for no-action relief.

Boards of Trade Located Outside of the United States and No-Action Relief From the Requirement To Become a Designated Contract Market or Derivatives Transaction Execution Facility, 71 Fed. Reg. 64,443, 64,446-47 (Nov. 2, 2006) (to be codified at 17 C.F.R. pt. 140) (footnotes omitted).

Exchange makes the following representations.

(1) Exchange represents that it has satisfied, and continues to satisfy, all the conditions established by the CFTC for the availability of the no-action relief from contract market designation.

(2) All Exchange contracts are subject to a system of marking to market whereby gains are credited to accounts and losses subjected to margin calls on a daily basis.

(3) Under Article 27 of the United States – United Kingdom Income Tax Treaty (2001), the Internal Revenue Service (the Service) may gain access to information held by Exchange with respect to U.S. taxpayers.

(4) Exchange will maintain an agent for service within the United States, to receive and accept any request for information, summons or subpoena from the Service or from any grand jury properly convened within the United States, which is related to the taxation of transactions in futures contracts traded on Exchange by any person.

(5) The supplying of records by Exchange to a U.S. grand jury or to the Service will not be a violation of, or inconsistent with, the law of the United Kingdom.

(6) Exchange will retain its records respecting futures trading on Exchange for five years.

(7) Exchange will collect from all Exchange Members their United States taxpayer identification numbers and will provide such information to the Service on request.

(8) Exchange will identify the executive officers of each Exchange Member and will make such information available to the Service on request.

(9) Exchange will provide such further information and assurances as may from time to time be requested by the Service in order to verify Exchange's entitlement to the determination under section 1256(g)(7)(C) of the Code.

(10) Exchange represents that the Exchange Regulations will be amended and approved to require the following.

a) With respect to the reporting requirements of brokers under section 6045 of the Code and the Treasury Regulations thereunder, Exchange Members who effect transactions on Exchange on behalf of persons, other than exempt foreign persons with respect to whom no return of information is required under section 1.6045-1(g) of the Treasury Regulations, will identify such persons and file returns in the manner prescribed by section 6045 of the Code, the regulations thereunder, and such other provisions of the Code and regulations that are pertinent thereto. Failure of an Exchange Member to comply with this provision will result in immediate

suspension of such Member's membership privileges on Exchange (and the privileges of any successor to such Member) until the member complies with these reporting requirements in all respects. Such compliance includes the filing of all returns that were required to have been filed under section 6045 but were not filed or were filed improperly.

b) In addition to the requirements of Exchange regulations, upon request by Exchange, Exchange Members (with respect to transactions occurring on Exchange) will supply to Exchange books, papers, records, or other data as described in section 7602 of the Code and the Treasury Regulations thereunder (hereinafter collectively referred to as "records"). Such requests will be made by Exchange whenever Exchange receives a written request, summons or subpoena to produce such records from the Service or from any grand jury.

Law and Analysis:

Section 1256(a) of the Code provides, in general, when gain or loss on section 1256 contracts will be recognized and how such gain or loss will be treated for federal income tax purposes.

Section 1256(b) of the Code provides, in part, that for purposes of this section, the term "section 1256 contract" means any regulated futures contract.

Section 1256(g)(1) of the Code provides that the term "regulated futures contract" means a contract (A) with respect to which the amount required to be deposited and the amount which may be withdrawn depends on a system of marking to market, and (B) which is traded on or subject to the rules of a qualified board or exchange.

Section 1256(g)(7) of the Code provides that the term "qualified board or exchange" means—

(A) a national securities exchange which is registered with the Securities and Exchange Commission,

(B) a domestic board of trade designated as a contract market by the Commodity Futures Trading Commission, or

(C) any other exchange, board of trade, or other market which the Secretary determines has rules adequate to carry out the purposes of this section.

Based on the foregoing, we determine that Exchange is a qualified board or

exchange within the meaning of section 1256(g)(7)(C). This determination is conditioned on the representations set forth above and compliance therewith. If the representations are not met or complied with, such determination will have no force or effect. This determination is also conditioned on Exchange's continued compliance with all CFTC conditions necessary to retain its no-action relief permitting it to make its electronic trading and matching system available in the United States, notwithstanding that Exchange is not designated as a contract market pursuant to Section 5 and 5a of the Commodity Exchange Act.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

/s/

Phoebe A. Mix
Special Counsel
(Financial Institutions & Products)