

## INSIGHTS

## CFTC Seeks Input on Dodd-Frank Implementation Issues Affecting Energy End-Users

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By: [George D. Fatula](#)

With most of its rules implementing the swap regulatory provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") in place, the Commodity Futures Trading Commission ("CFTC") is seeking new public input on several aspects of its Dodd-Frank rules that directly affect energy markets participants who use swaps to hedge risk or who transact physical agreements containing options that are subject to the swap regulations. Entities that utilize swaps and options in this manner, but are not otherwise required to register with the CFTC as "swap dealers" or other regulated entities, are referred to as "end-users." the first such initiative, on April 3, 2014 the CFTC's staff will host a public roundtable to discuss issues concerning end-users with respect to Dodd-Frank regulations that have raised questions and requests for clarification with the CFTC and its staff. In particular, this roundtable will cover the scope of the CFTC's definition of the term "swap," which was defined in a lengthy interpretation issued in August 2012. That scope has included many physical transactions, particularly those involving power, gas, oil and other energy commodities, that require physical delivery of some minimum quantity but that also feature some form of "volumetric optionality"; that is, one or both parties have the ability to vary the quantity that is bought/sold. For example, many natural gas purchase and sale agreement confirmations require the buyer to nominate between a minimum and a maximum quantity for each month of delivery. Under the CFTC's interpretation of the term "swap," such an agreement could be a "commodity option" (synonymous with "swap") unless the exercise of that volumetric optionality is tied to some factor outside the parties' control. This interpretation has led to wide-spread confusion and uncertainty in physical energy markets as to whether physical purchase and sale agreements are properly included within the CFTC's swap definition. Questions and uncertainty have also spread as to the extent of regulatory requirements applicable to physical-delivery agreements that are captured by the swap definition, since they may also qualify for a lesser regulatory treatment if they fall into another category of swaps called "trade options." End-users are generally not required to shoulder the burden of swap reporting with respect to their financial swap transactions with financial institutions and others who are registered as "swap dealers" with the CFTC, but the broad and uncertain reach of the regulations into purely physical transactions has left many with unanswered questions about their regulatory responsibilities, and consensus in the markets has proven elusive in the absence of definitive guidance. Another issue to be addressed at the April 3 roundtable is the

appropriate treatment of certain swap transactions with government utilities. Under the CFTC's regulations implementing Dodd-Frank, entities are required to register and submit to stringent regulation as "swap dealers" if they engage in more than *de minimis* amount of "swap dealing." Swap dealing is understood to include providing hedges through swaps with entities that are using the swaps to hedge commercial risk, and the CFTC has set a *de minimis* threshold for swap dealing with government entities of \$25 million per year. This relatively low threshold has made it difficult for government utilities and other similar entities to find hedge counterparties other than large financial institutions, since other end-users are reluctant to engage in swap dealing with them and thus trigger the swap dealer definition. While the CFTC staff has recently extended existing no-action relief that has mitigated this risk to some extent, the roundtable discussion will include input on how this issue should be addressed going forward. The roundtable will seek input and discussion from market participants and counsel on these and other issues, including the scope of CFTC recordkeeping obligations for end-users trading on swap execution facilities. In another move to seek public input on Dodd-Frank implementation, the CFTC has also recently requested public comment on its existing swap data recordkeeping and reporting rules, which took effect under a phased implementation schedule through the spring and summer of 2013. Now that those rules are in place, the CFTC has asked for comment on approximately 70 different questions covering the content of required swap data reports, timing of reports, the utility of the reported information in presenting an accurate picture of swap transactions, and other topics. Energy market end-users are subject to the swap data reporting and recordkeeping rules, and will have an opportunity to point out issues, problems and potential improvements in the rules now that they have had nearly a year to experience and comply with the new requirements. Comments are due or before May 27, 2014. These CFTC initiatives to seek public input on specific aspects of the Dodd-Frank implementation regime demonstrate that nearly four years after the statute was signed into law, and with most of the regulatory architecture in place, compliance issues and uncertainty about the scope and coverage of the requirements remain. End-users will use these opportunities to both highlight problems that they face in designing processes and programs to implement Dodd-Frank compliance, and suggest solutions to streamline the compliance process going forward.