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CFTC Advisory Committee Reviews Position Limits Proposal, Reopens Public Comments until March 28, 2015

On February 25, 2015, the Commodity Futures Trading Commission (CFTC or Commission) published a notice that it would reopen the comment period for its previously proposed rule to establish speculative position limits for 28 exempt and agricultural commodity futures and options contracts, and the physical commodity swaps that are economically equivalent to such contracts ("Position Limits Proposed Rule"). The reopening of the public comment period was set to coincide with the February 26, 2015 Commission Energy and Environmental Markets Advisory Committee (EEMAC) public meeting, chaired by CFTC Commissioner J. Christopher Giancarlo, which considered, among other matters, exemptions for bona fide hedging positions.

This publication briefly explores the procedural history behind the Position Limits Proposed Rule and the discussion at the recent EEMAC meeting.

Background – Position Limits Proposed Rule

The position limits regime is governed by Section 4a of the Commodity Exchange Act (CEA). In 2010, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), which amended the CEA to authorize the Commission to establish position limits not just for futures and option contracts, but also for swaps that are economically equivalent to covered futures and options contracts, swaps traded on a designated contract market (DCM) or swap execution facility (SEF), swaps that are traded on or subject to the rules of a DCM or SEF, and swaps not traded on a DCM or SEF that perform or affect a significant price discovery function with respect to regulated entities ("SPDF Swaps").

On January 26, 2011, the CFTC initially published its proposed position limits regime, which was ultimately adopted as a final rule on October 18, 2011 ("First Final Rule") by a three to two vote. Subsequently, the First Final Rule was challenged in federal court by the International Swaps and Derivatives Association and Securities Industry and Financial Markets Association and ultimately vacated and remanded to the Commission by Judge Robert Wilkins of the US District Court for the District of Columbia. In granting the plaintiffs' motion for summary judgment, Judge Wilkins found that the CEA provision allowing the CFTC to promulgate limits "as the [CFTC] finds are necessary" did not mandate CFTC-implemented position limits and first required that the CFTC first conclude such position limits were necessary before promulgating the regulation. Because the CFTC did not first reach the formal conclusion that position limits were necessary, the First Final Rule was vacated and remanded to the Commission. The CFTC did not appeal the decision.

Subsequently, on November 15, 2013, the CFTC published a notice of proposed rulemaking ("Aggregation Proposal") to amend existing regulations setting out the Commission's policy for aggregation under its position limits regime. Following this notice, on December 12, 2013, the CFTC published a second notice of proposed rulemaking to establish speculative position limits for exempt and agricultural commodity futures and options contracts, and the physical commodity swaps that are economically equivalent to such contracts (the previously-referenced "Position Limits Proposed Rule").

The Commission intentionally adopted the Aggregation Proposal and the Position Limits Proposed Rule separately given its belief that the proposed amendments regarding aggregation of positions would be appropriate regardless of whether the Position Limits Proposed Rule was adopted. However, given that the comment period for both proposals lasted for 60 days after publication in the *Federal Register*, coupled with the fact that the Aggregation Proposal was published earlier than the Position Limits Proposed Rule, the CFTC, on January 14, 2014, extended the comment period for the Aggregation Proposal for the duration of the comment period for the Position Limits Proposed Rule, which ended on February 10, 2014. The Commission's reasoning for this extension was to provide interested parties with an opportunity to comment on the Aggregation Proposal for so long as the comment period on the Position Limits Proposed Rule remained open.

Since then, the Commission has extended the comment period on the proposals four times.

On June 19, 2014, Commission staff held a public roundtable to consider certain issues regarding position limits for physical commodity derivatives. In order to provide interested parties with an opportunity to comment on the issues discussed at the roundtable, the Commission reopened the comment periods for the Aggregation Proposal and Position Limits Proposed Rule for a three-week period starting June 12, 2014 (one week before the roundtable), and ending July 3, 2014 (two weeks following the roundtable). The CFTC then provided an additional extension through August 4, 2014, to provide commenters with a sufficient period of time to respond to specific issues stemming from the roundtable related to hedges of a physical commodity by a commercial enterprise, including: (1) gross hedging; (2) cross-commodity hedging; (3) anticipatory hedging; and (4) the process for obtaining a non-enumerated exemption. The CFTC also sought comment on other specific issues, including: (1) the setting of spot month limits in physical-delivery and cash-settled contracts and a conditional spot-month limit exemption; (2) the setting of non-spot limits for wheat contracts; (3) the aggregation exemption for certain ownership interests of greater than 50% in an owned entity; and (4) aggregation based on substantially identical trading strategies.

On December 9, 2014, the Commission's Agricultural Advisory Committee held a public meeting to consider, among other topics, deliverable supply and exemptions for bona fide hedging positions. To provide commenters with a sufficient period to respond to issues arising at the Agricultural Advisory Committee meeting, the Commission reopened the comment periods for an additional 45 days (from December 9, 2014 to January 22, 2015) and limited commenters to commenting on the following issues as they pertain to agricultural commodities: (1) hedges of a physical commodity by a commercial enterprise and (2) the process for estimating deliverable supplies used in the setting of spot month limits.

CFTC EEMAC Explores Bona Fide Hedging

Most recently, on February 26, 2015, the Commission's EEMAC held a meeting to consider, among other topics, exemptions for bona fide hedging positions. Commissioner J. Christopher Giancarlo, who sponsors the EEMAC, indicated that energy industry representatives have "impressed [ ] their deep concern over the form and substance of the Commission's proposed position limits regime on energy derivatives" and that "exploring the unique concerns of energy market participants regarding the position limits proposals will ensure that the Commission has a complete picture of the consequences of these proposals on all aspects of the energy and environmental markets." By contrast, Commissioner Sharon Bowen reiterated her prior remarks that the Commission should finalize and adopt the Position Limits Proposed Rule in 2015.

On the same day as the EEMAC meeting, Chairman Timothy Massad spoke before the Coalition for Derivatives End-Users, stating that "Congress mandated that we implement position limits to address the risk of excessive speculation. In doing so, we must make sure that commercial end-users can continue to engage in bona fide hedging." He noted that the CFTC has "received substantial public input on the position limits rule" and the Commission must "consider these comments carefully."

The EEMAC meeting reviewed research and data related to the Position Limits Proposed Rule, considered liquidity on DCMs on previously-established position limits, and explored the bona fide hedging exemption.

To ensure that commenters had sufficient time to respond to issues resulting from the EEMAC meeting and the counts of those entities over the 28 proposed position limits, the CFTC reopened the comment periods for an additional 30 days, running from February 26, 2015, through March 28, 2015.

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