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LEGAL ALERT

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CFTC Proposes Position Limits for Major Energy Commodities

Today, the U.S. Commodity Futures Trading Commission (CFTC), in a fairly unprecedented public hearing, approved publication of a proposed rule to set position limits for futures and option contracts in the major energy markets. The proposal would cover four energy commodity contracts: (1) the NYMEX Henry Hub natural gas contract; (2) the NYMEX Light Sweet crude oil contract; (3) the NYMEX New York Harbor No. 2 heating oil contract; and (4) the NYMEX New York Harbor gasoline blendstock (RBOB) contract. The rule would also apply to any other contract that is exclusively or partially based on the referenced contracts' commodities and is deliverable at locations specified in the proposed regulations. Currently, these products are traded on two CFTC-regulated exchanges: (1) the New York Mercantile Exchange (NYMEX) and (2) the Intercontinental Exchange (ICE).

As indicated in the CFTC's fact sheet and Q&A regarding the proposed rulemaking, the proposal seeks to build upon the CFTC's experience in setting position limits for specified agricultural products. Another important aspect of the proposed rulemaking is the proposed exemptions for bona fide hedging and a new limited risk management exemption for swap dealers, in lieu of an exemption for a bona fide hedging transaction. According to the CFTC Q&A, the proposed rulemaking, if finalized, would likely affect approximately ten large traders. These large traders could seek and may qualify for exemptions.

The proposed rule would *not* limit trading in the over-the-counter (OTC) market and this was a factor in Commissioner Sommers' decision to dissent from approval of the proposed rulemaking. Other factors cited by Commissioner Sommers include the current consideration in Congress of legislation that would specifically authorize the CFTC to establish position limits for both the regulated futures markets and the OTC market, and her view that the proposed rule's impact on large, passive investors has not been adequately analyzed nor has the risk posed by such large investors been clearly demonstrated. Commissioner Dunn, while approving publication of the proposed rule, voiced "serious reservations" about the proposal and indicated that his vote should not be interpreted as his agreement with the proposal. Commissioner O'Malia and Commissioner Dunn expressed concern that imposing limits on the regulated futures markets without also regulating the OTC market would be an uncoordinated effort that is not likely to achieve the goal of curbing speculation or avoiding manipulation in the futures markets.

Given the three Comissioners' skepticism, much remains to be seen as to how the final rule will look. When a final rule would be issued is also uncertain. In addition to the announced public comment period, it was suggested during the hearing that the evaluation period could extend over a lengthy period of time. Additionally, Congress is looking at the same issue contemporaneously, and the legislative process can be anticipated to have an impact on the issuance of a final rule.

The following is a link to the text of the CFTC's proposed rule on position limits: http://www.futuresindustry.org/files/Federal_Speculative_Position_Limits_for_Referenced_Energy_Contract_and_Associated_Regulations_011410.pdf. There will be a 90-day public comment period commencing on the day the proposed rulemaking is published in the Federal Register.

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If you have any questions regarding this Legal Alert, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

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