

MEMO# 23416

April 24, 2009

CFTC Issues Concept Release on Whether to Eliminate the Bona Fide Hedge Exemption for Swap Dealers

[23416]

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TO:

SEC RULES COMMITTEE No. 19-09
EQUITY MARKETS ADVISORY COMMITTEE No. 18-09
ETF ADVISORY COMMITTEE No. 10-09

RE:

CFTC ISSUES CONCEPT RELEASE ON WHETHER TO ELIMINATE THE BONA FIDE HEDGE
EXEMPTION FOR SWAP DEALERS

The Commodity Futures Trading Commission (“CFTC” or “Commission”) has published a concept release in the form of an advanced notice of proposed rulemaking seeking comment on whether to eliminate the bona fide hedge exemption for swap dealers and replace it with a more limited risk management exemption (“Release”).[\[1\]](#) The new limited risk management exemption may be conditioned upon, among other things, an obligation to report to the CFTC and applicable self-regulatory organizations when certain noncommercial swap clients reach a specified position level and/or a certification that none of a swap dealer’s noncommercial swap clients exceed specified position limits in related exchange-regulated commodities. The Release was issued in response to a prior

recommendation contained in a September 2008 CFTC Staff Report.[\[2\]](#)

The Release reviews the statutory and regulatory background for CFTC and exchange speculative position limits, existing exemptions from the limits, and relevant market developments that led to the Staff Report. In particular, the Release discusses the bona fide hedge exemptions that were granted by the CFTC staff to a number of swap dealers for positions in exchange-traded futures contracts on certain agricultural commodities entered into to offset risks related to swaps or similar over-the-counter positions involving both individual commodities and commodity indexes.[\[3\]](#) In a footnote, the Release also notes that Commission staff in 2006 issued two no-action letters with respect to trading that offered investors the opportunity to participate in a broadly diversified commodity index-based fund or program.[\[4\]](#) The letters state that enforcement action will not be taken for violations of certain Commission speculative position limits, provided that the requesting party complies with certain conditions, because the index fund positions represent a legitimate and potentially useful investment strategy.

The CFTC has requested general views and comments regarding the appropriate treatment of swap dealers with respect to existing bona fide hedge exemptions, as well as responses to a number of specific questions regarding (i) the advisability of eliminating the exemption for swap dealers, (ii) the terms of a potential new limited risk management exemption for swap dealers, and (iii) how the two index traders who have received no-action relief from Federal speculative position limits should be treated under any new regulatory scheme.

Comments on the Release are due by May 26, 2009. If there are issues you would like the Institute to consider addressing in a comment letter, please contact Ari Burstein at 202-371-5408 or aburstein@ici.org or Eva Mykolenko at 202-326-5837 or emykolenko@ici.org.

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endnotes

[1] See Concept Release on Whether To Eliminate the Bona Fide Hedge Exemption for Certain Swap Dealers and Create a New Limited Risk Management Exemption From Speculative Position Limits, 74 Fed. Reg. 12282 (March 24, 2009), available at <http://www.cftc.gov/stellent/groups/public/@lrfederalregister/documents/file/e9-6187a.pdf>.

[2] See Staff Report on Commodity Swap Dealers and Index Traders with Commission Recommendations, available at <http://www.cftc.gov/stellent/groups/public/@newsroom/documents/file/cftcstaffreportonswapdealers09.pdf> ("Staff Report"). The Staff Report contains several preliminary Commission recommendations, which are based on a summer 2008 special call for information from swap dealers and index traders regarding their over-the-counter market activities.

[3] The exemptions granted by the CFTC staff apply only to the agricultural commodities that are subject to Federal speculative position limits specified in Commission Regulation 150.2.

[4] See CFTC Letter 06-09, April 19, 2006, available at <http://www.cftc.gov/stellent/groups/public/@lrfletter06/documents/letter/06-09.pdf> and CFTC Letter 06-19, September 6, 2006, available at <http://www.cftc.gov/stellent/groups/public/@lrfletter06/documents/letter/06-19.pdf>.

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