

CFTC Solicits Comments on How the Trading of Agricultural Swaps Should Be Governed

October 20, 2010

On September 28, 2010, the Commodity Futures Trading Commission (CFTC) issued an Advanced Notice of Proposed Rulemaking ([ANPRM](#)) requesting public comments on the appropriate conditions, restrictions, or protections that should be included in any CFTC rule, regulation or order governing the trading of “agricultural commodity” swaps.¹

With respect to swaps generally, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) directs the CFTC to determine, based on certain factors, whether a swap, or a group, category, type, or class of swaps, should be required to be cleared. To the extent that a swap transaction is required to be cleared, such swap must be executed on a designated contract market (DCM) or a swap execution facility (SEF).² Swaps that are not subject to the clearing requirement may be executed bilaterally over-the-counter. In addition, swaps entered into by “commercial end-users” (non-financial entities that use swaps to hedge or mitigate commercial risk) will not be subject to mandatory clearing and may be executed bilaterally over-the-counter.

Notwithstanding these general swap provisions, however, with respect to agricultural commodity swaps, even though such swaps fall under the definition of “swap” contained in Dodd-Frank, **Section 723(c)(3) of Dodd-Frank explicitly prohibits swaps in agricultural commodities unless they are entered into pursuant to a CFTC rule, regulation, or order granted under Section 4(c) of the Commodity Exchange Act.**³ As a result, it is unclear whether agricultural commodity swaps will be subject to the comprehensive regulatory framework that Dodd-Frank establishes for swaps or to a different regulatory framework adopted by the CFTC. Importantly, pursuant to its authority under Section 723(c)(3) of Dodd-Frank, the CFTC may impose a variation of this regulatory framework on agricultural swaps, or it may adopt completely distinct requirements for them.

Because of the uncertainty surrounding how the CFTC will regulate agricultural commodity swaps, market participants that engage in such swaps and options transactions may wish to submit comments in response to the ANPRM in order to participate in the CFTC rulemaking at its earliest stages. The deadline for submitting comments in response to the ANPRM is **October 28, 2010**.

¹ Importantly, the term “agricultural commodity” has not yet been defined. This definition is obviously critical to how broadly the CFTC’s rules will ultimately extend. On October 19, 2010 the CFTC issued a release seeking public comment on the definition of an “agricultural commodity” (for further information on this release see Sutherland’s Legal Alert dated October 19, 2010, “[CFTC Proposed Rulemaking to Cover How Biofuels Should be Regulated](#)”); in the interim, the ANPRM directs members of the public submitting comments to assume that “agricultural commodity” includes: (1) the enumerated commodities in Section 1a(4) of the CEA; (2) international “soft commodities”; (3) lumber, plywood and similar wood-derived commodities; (4) contracts based on any of the foregoing; and (5) other commodities derived from living organisms that are currently the subject of derivatives trading.

² CFTC regulations pertaining to DCMs and SEFs are forthcoming.

³ Agricultural commodity swaps are currently governed by Part 35 of the CFTC’s rules, and options on agricultural commodities are currently permissible under Part 32 of the CFTC’s rules. While Dodd-Frank provides that those agricultural commodity swaps (not options) meeting the Part 35 rules that were in place before Dodd-Frank was enacted will continue to be permitted pursuant to a “grandfather clause,” the post-Dodd-Frank regulatory reforms might well revise such current regulations substantially.

The ANPRM requests that public comments address (among other things): the current agricultural swaps business, the potential effect of requiring agricultural swaps to be cleared under the Dodd-Frank clearing regime, pros and cons of permitting agricultural swaps to be cleared on DCMs or SEFs, and the pros and cons of permitting agricultural swaps to be traded outside of DCMs and SEFs to a different extent than other types of swaps. Commenters may also wish to focus on why agricultural swaps should or should not be treated like other swaps, and the effect that prohibiting agricultural swaps may have on risk mitigation by agricultural market participants. Recently senior CFTC officials have indicated that for comments to receive meaningful consideration, they should identify specific adverse effects that a particular rule or prohibition would have on industry trading practices and/or participants.

The full list of issues on which the CFTC is requesting comment may be found in the [ANPRM](#). Comments should be submitted to the CFTC either electronically (by e-mail to agswapsANPR@cftc.gov) or in hard copy form (either by mail or hand-delivery).

Please contact one of the Sutherland attorneys listed below if you would like more information about the CFTC's regulation of agricultural swaps or if you would like advice on, and/or assistance in, preparing comments in response to the ANPRM.

We will continue to monitor the implementation of the Dodd-Frank Act through the rulemaking process and will keep you updated on key events.



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

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