



December 16, 2022

Christopher J. Kirkpatrick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, N.W.  
Washington, DC 205891

**RE: Petition of the Futures Industry Association, Inc. and the International Swaps and Derivatives Association, Inc. for a Commission Determination Concerning the Definition of Economically Equivalent Swap**

Dear Mr. Kirkpatrick:

The Futures Industry Association, Inc. (“**FIA**”) and the International Swaps and Derivatives Association, Inc. (“**ISDA**”) (collectively, the “**Associations**”) respectfully petition the Commission to determine, pursuant to its existing authority in the position limits rule (the “**Position Limits Rule**”), whether the swaps described herein meet the requirements of the definition of economically equivalent swap.<sup>1</sup> The Commission expressly retained the authority to make the determination requested by the Associations in the text of the definition of economically equivalent swap.<sup>2</sup> The Associations are not requesting that the Commission substantively amend the definition, which as explained below is clear on its face, through notice and comment rulemaking.

Subpart 3 of the economically equivalent swap definition provides that “[w]ith respect to any referenced contract or class of referenced contracts, the Commission may make a determination that any swap or class of swaps satisfies, or does not satisfy, this economically equivalent swap definition.”<sup>3</sup> The Commission adopted this provision so it would be able “to offer clarity to the marketplace in cases where uncertainty exists as to whether certain swaps would qualify (or would not qualify) as ‘economically equivalent,’ and therefore would be (or would not be) subject to Federal position limits.”<sup>4</sup> The Associations request that the

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<sup>1</sup> *Position Limits for Derivatives*, 86 Fed. Reg. 3236 (Jan. 14, 2021) (“**Position Limits Rule**”).

<sup>2</sup> Regulation 150.1, 17 C.F.R. 150.1 (definition of “economically equivalent swap”).

<sup>3</sup> *Id.*

<sup>4</sup> *Position Limits Rule*, 86 Fed. Reg. at 3295. Furthermore, in the preamble to the Position Limits Rule, the Commission explained that “a market participant could petition, or request informally, that the Commission make . . . a determination” that a swap or class of swaps satisfies or does not satisfy the definition of an economically equivalent swap. *Id.* at 3415.

Commission determine whether the swaps described herein are economically equivalent swaps because market participants need certainty in order to identify and monitor contracts subject to federal limits, and to comply with the Position Limits Rule.

As we explain below, an FIA position limits working group (“**Working Group**”), many members of which also are members of ISDA, followed the process specified by the Commission in the preamble to the Position Limits Rule to make a reasonable, good faith determination that the swaps described herein do not satisfy the definition of economically equivalent swap. However, FIA recently received an informal communication from the Division of Market Oversight (“**DMO**”) which indicates that DMO Staff disagrees in part with the determinations of the Working Group. As a result, uncertainty exists as to whether certain swaps are economically equivalent swaps and, therefore, subject to federal position limits. Having received DMO’s different informal view about the scope of the definition, members of the Working Group and the Associations need the Commission’s guidance concerning how to apply the Position Limits Rule and the preamble to make a reasonable, good faith determination that a swap or class of swaps is or is not an economically equivalent swap. Any determination made by the Commission in response to this Petition will provide clarity to all market participants, many of which are not members of the Associations and, absent this Petition, may be unaware of DMO’s informal position.

## **I. The Interests of the Associations and the Position Limits Working Group**

### **A. The Futures Industry Association**

FIA is the leading global trade organization for the futures, options and centrally cleared derivatives markets, with offices in Brussels, London, Singapore and Washington, D.C. FIA’s membership includes clearing firms, exchanges, clearinghouses, trading firms and commodities specialists from about 50 countries, as well as technology vendors, lawyers and other professional service providers. FIA’s mission is to support open, transparent and competitive markets; protect and enhance the integrity of the financial system; and promote high standards of professional conduct. As the principal members of derivatives clearinghouses worldwide, FIA’s clearing firm members play a critical role in the reduction of systemic risk in global financial markets. On behalf of its members, FIA has commented on all of the Commission’s proposed rules related to federal position limits.

### **B. The International Swaps and Derivatives Association**

Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 1,000 member institutions from 79 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other

service providers. On behalf of its members, ISDA has commented on all of the Commission’s proposed rules related to federal position limits.

### **C. The FIA Position Limits Working Group**

The Working Group has met regularly since publication of the Position Limits Rule to assist firms in understanding and taking steps to comply with the Position Limits Rule. The Working Group is comprised of legal, compliance and operations representatives of approximately 70 FIA member firms, including producers, marketers, commercial end-users, swap dealers, FCMs, futures exchanges, law firms and consulting firms. The Working Group meets to discuss issues of common interest to persons subject to, and best practices for complying with, federal and exchange position limits. One of the topics, among many, that the Working Group has addressed is the scope of swaps that fall within the definition of economically equivalent swap in Regulation 150.1. As the Commission is aware, the compliance date when economically equivalent swaps will be subject to federal position limits is January 1, 2023.

### **D. The Working Group Followed the Commission’s Recommended Process for Determining Whether Swaps Are Economically Equivalent Swaps**

In the preamble to the Position Limits Rule, the Commission explained that determining whether a swap is economically equivalent to a particular referenced futures contract requires “a facts and circumstances analysis.”<sup>5</sup> For this reason, and because “most physical commodity swaps are created bilaterally between counterparties and traded” in the over-the-counter (“OTC”) market, the Commission declined to publish a list of swaps that are economically equivalent to referenced futures contracts.<sup>6</sup> Instead, the Commission emphasized that it “believes that market participants are best positioned to determine whether particular swaps share identical material terms with referenced contracts and would therefore qualify as ‘economically equivalent’ for purposes of Federal position limits.”<sup>7</sup> Market participants have decades of experience negotiating and documenting the contractual terms of OTC swap agreements either pursuant to industry standard forms and definitions, or bespoke contracts. Given this experience, the Commission provided market participants with the discretion to determine in the first instance whether a swap is economically equivalent to a particular referenced futures contract “as long as market participants make a reasonable, good faith effort in reaching their determination and are able to provide sufficient evidence, if requested, to support a reasonable, good faith effort.”<sup>8</sup>

The Commission also provided market participants with a safe harbor against an enforcement action as long as they satisfy two conditions when determining whether a swap is an economically equivalent swap. A market participant must: “(i) perform[] the necessary due

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<sup>5</sup> *Id.* at 3295.

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>8</sup> *Id.* at 3415.

diligence and [be] able to provide sufficient evidence, if requested, to support its reasonable, good faith determination that the swap is or is not an economically equivalent swap and (ii) [if the Commission makes a contrary determination,] come[] into compliance with the applicable Federal position limits within a commercially reasonable time, as determined by the Commission in consultation with the market participant, and if applicable, any relevant exchange.”<sup>9</sup> When it issued the Position Limits Rule, the Commission stated that this approach should provide market participants with “a greater level of certainty” rather than first submitting “swaps to the Commission staff and wait[ing] for feedback before entering into swaps.”<sup>10</sup>

Following the Commission’s direction, the Working Group endeavored to perform reasonable due diligence to make good faith equivalence determinations about the swaps discussed herein. The Working Group’s goal in undertaking this effort was to ensure that they could develop and implement policies and procedures reasonably designed to comply with upcoming position limits on economically equivalent swaps based upon the text of the definition and the Commission’s explanation of how to apply the definition in the preamble to the Position Limits Rule. It did not seek either a pre-determined outcome or to benefit any particular type of market participant or any particular designated contract market (“**DCM**”).

As part of the Working Group’s effort, FIA retained outside counsel to analyze the facts, circumstances and applicable law necessary to determine whether certain swaps fall within or outside the definition of economically equivalent swap. At the direction of the Working Group, outside counsel reviewed the text of the definition and the Commission’s explanation of the definition in the preamble to the rule. Next, counsel reviewed sample swap agreement confirmations across several commodity asset classes provided by members of the Working Group. The confirmations were redacted to remove counterparty identifying information, but otherwise contained or incorporated by reference all of the material contractual terms of the swap. Finally, counsel compared the material contractual specifications, terms, and conditions of the swaps to the material contractual specifications, terms, and conditions of the particular futures contract specified in the swaps to determine whether they were identical. The results of counsel’s factual and legal analysis are set forth in the July 14, 2022 memorandum attached hereto as **Exhibit 1** (the “**Working Group Memorandum**”). Based upon the detailed factual and legal analysis set forth in the Working Group Memorandum, and in consultation with the

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<sup>9</sup> *Id.* at 3295. The CFTC further explained that “[a]s long as the market participant made its determination, prior to such Commission determination, using reasonable, good faith efforts, *the Commission would not take any enforcement action* for violating the Commission’s position limits regulations if the Commission’s determination subsequently differs from the determination of the market participant and the market participant comes into compliance with the applicable Federal position limits within a commercially reasonable time. . . .” *Id.* at 3295 n.437 (emphasis added).

<sup>10</sup> *Id.* at 3295; *see also id.* at 3415 (“The Commission anticipates that *this flexibility will benefit market integrity* by providing a greater level of certainty to market participants, in contrast to the alternative in which market participants would be required to first submit swaps to the Commission staff and wait for feedback or approval.” (Emphasis added)).

Working Group, counsel concluded that the swaps listed in **Appendix A** thereto reasonably and in good faith should be characterized as outside the definition of economically equivalent swap.<sup>11</sup>

## **II. The Associations Are Uncertain About How to Determine Whether a Swap is an Economically Equivalent Swap in Light of DMO's Informal Communication**

After learning indirectly that Staff in DMO might have a different view than the Working Group concerning the scope of the definition of economically equivalent swap, representatives of FIA met with DMO staff on July 13, 2022, to discuss the Working Group's analysis. Prior to the meeting, FIA provided DMO staff with a draft of the Working Group Memorandum. During the meeting, FIA representatives explained that the Working Group had determined that a cash-settled swap that uses as its Commodity Reference Price a physically-settled core referenced futures contract does not fall within the definition of an economically equivalent swap. Although DMO Staff noted that they were not speaking in an official capacity, they suggested that such a swap could be an economically equivalent swap if a look-a-like financially-settled referenced futures contract exists. DMO Staff said they would provide further information on their view after the meeting.

On September 22, 2022, FIA provided DMO Staff with the final version of the Working Group Memorandum. The final version addressed issues that FIA representatives discussed with DMO Staff during the July 13, 2022 meeting.

FIA understands from a recent informal communication from DMO that Staff disagrees in part with the determinations in the Working Group Memorandum. In particular, DMO Staff stated that they "consider swaps to be economically equivalent under the definition set forth in Reg[.] 150.1 to the extent that the swap *mirrors* the terms of a cash-settled look-alike futures contract (that is, a swap that by definition copies all material terms of the corresponding future)." According to Staff, "the economically equivalent swap definition explicates that a swap may be deemed to be economically equivalent to *any referenced contract*."<sup>12</sup> DMO Staff further stated that "if a swap mirrors a financially-settled look-alike future, the swap by definition shares all material terms – including the commodity reference price – and is considered an economically equivalent swap *to that financially-settled look-alike future* (but the financially-settled swap is not deemed to be an EE swap to the physically-settled core referenced futures contract underlying the look-alike future)."<sup>13</sup>

For the reasons explained below, DMO's informal communication concerning the definition of economically equivalent swap creates ambiguity concerning how market participants should read the text of the definition and the Commission's explanation in preamble to make a reasonable, good faith determination about whether a swap is an economically equivalent swap. DMO's use of the term "mirror," particularly with respect to the price term of the two contracts, focuses on price linkage. Consequently, it equates the definition of

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<sup>11</sup> All references to Appendices herein are to the Appendices to the Working Group Memorandum.

<sup>12</sup> Emphasis by Staff.

<sup>13</sup> Emphasis by Staff.

economically equivalent swap with the definition of referenced contract—something the Commission expressly declined to do.<sup>14</sup> As a result, the Associations are unable to reconcile DMO’s informal communication with the rule text, the Commission’s statements in the preamble and the process outlined by the Commission for determining whether a swap is an economically equivalent swap, *i.e.*, whether the swap and the particular futures referenced contract have “identical” material contractual terms.

Because DMO’s informal communication is not based upon the definition of economically equivalent swap or the Commission’s explanation of the definition in the preamble, it does not provide market participants with objective metrics against which to analyze a swap to determine whether it falls within the scope of the definition. Moreover, it is contrary to the Commission’s statements regarding the ability of market participants to make reasonable, good faith judgments in applying the definition of economically equivalent swaps. Market participants need a determination by the Commission concerning how to identify economically equivalent swaps in order to develop the surveillance systems necessary to monitor their swap and related futures positions for compliance with both federal and exchange position limits.

### **III. The Text of the Position Limits Rule and the Commission’s Guidance**

#### **A. Interpreting The Definition of Economically Equivalent Swap**

The Working Group and counsel examined the text and structure of the Position Limits Rule and its purpose as reflected in the preamble in assessing the scope of the definition of economically equivalent swap.<sup>15</sup> In the Working Group’s view, the definition and the Commission’s explanation of the rule are not ambiguous. Consequently, the Working Group believes that its interpretation is reasonable and fully consistent with the Commission’s statements, and that an alternative interpretation is not supported by either the rule text, structure

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<sup>14</sup> Position Limits Rule at 3302 n.493 (“As discussed above, the Commission adopted an ‘economically equivalent swap’ definition that is narrower than the class of futures contracts and option on futures contracts that would be included as referenced contracts.”).

<sup>15</sup> The Supreme Court has held that, when interpreting federal agency regulations, “court[s] must ‘carefully consider[.]’ the text, structure, history and purpose of a regulation. . . .” *Kisor v. Wilkie*, 139 S. Ct. 2400, 2415 (2019); *see also Dresser-Rand Co. v. Petroleos de Venezuela, S.A.*, 574 F. Supp. 3d 217, 223-24 (S.D.N.Y. 2021). Only if a regulation is ambiguous should a court conduct an independent analysis of whether an agency’s interpretation of its own regulation is reasonable and entitled to controlling weight. *Kisor*, 139 S. Ct. at 2415. As a prerequisite to the validity of regulations, the APA requires every agency, including the Commission, to “incorporate in the rules adopted a concise general statement of their basis and purpose,” *i.e.*, the preamble to the rule. 5 U.S.C. § 553(c). In the Commission’s statement of the “basis and purpose” of the definition of economically equivalent swap, it noted that because the CEA “does not define the term ‘economically equivalent,’ the Commission is applying its expertise in construing such term consistent with the policy goals articulated by Congress, including in CEA sections 4a(a)(2)(C) and 4a(a)(3) . . . .” Position Limits Rule, 86 Fed. Reg. at 3413. The basis and purpose of a regulation can be “discerned from the regulation’s text and accompanying explanatory material. . . .” Andrew Edgar & Kevin M. Stack, *The Authority and Interpretation of Regulations*, 82 Modern L. Rev. 1009, 1010 (Nov. 2019). The Second Circuit similarly has explained that regulatory interpretation requires an “examin[ation] [of] the regulation’s text in light of its purpose, as stated in the regulation’s preamble.” *Halo v Yale Health Plan Dir. Of Benefits & Records Yale Univ.*, 819 F.3d 42, 52 (2d Cir. 2016), cited in *The Authority and Interpretation of Regulations*, at 1026.

of, or preamble to, the Position Limits Rule. ISDA supports the Working Group’s economically equivalent swap determinations in Exhibit 1, and agrees that they are reasonable and were made in good faith.

A broader interpretation of the definition of economically equivalent swap would have several unintended consequences, all of which would be contrary to the Commission’s express intent that the definition apply only to a narrow class of swaps. It would, among other things, significantly expand the scope of swaps and classes of swaps subject to position limits, which in turn would increase the compliance burden on market participants. Expanding the scope of economically equivalent swaps would also produce a number of outcomes that the Commission said it was seeking to avoid in adopting the rule, including enabling more opportunities for netting and incentivizing regulatory arbitrage.

## **B. The Commission Intentionally Adopted a Narrow Definition of Economically Equivalent Swap**

The Commission stated in the preamble that it intentionally adopted a narrow definition of economically equivalent swap. Based upon a careful review of the statutory framework for setting federal speculative position limits, the Commission explained that “Congress’s underlying policy goals in CEA section 4a(a)(2)(C) and (3)(B) are best achieved by *adopting a narrow definition of ‘economically equivalent swap,’* compared to the broader definition of ‘referenced contract.’”<sup>16</sup> According to the Commission, “the relatively narrow definition supports the statutory objective in CEA section 4a(a)(2)(C) by not causing price discovery to shift to trading in foreign markets.”<sup>17</sup> Furthermore, the narrow definition of economically equivalent swap “supports the statutory objectives in CEA section[s] 4a(a)(3)(B)(i) and (ii) by helping to prevent excessive speculation and market manipulation, including corners and squeezes, respectively, by: (1) [f]ocusing on swaps that are the most economically equivalent in every significant way to the futures contracts and options on futures contracts for which the Commission deems position limits to be necessary; and (2) limiting the ability of speculators to obtain excessive positions through netting.”<sup>18</sup>

The Commission explicitly declined to adopt a broader definition of economically equivalent swap as requested by some commenters.<sup>19</sup> The Commission’s primary objective in adopting a narrow definition was to prevent “parties from using netting of swaps to create large

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<sup>16</sup> Position Limits Rule at 3289 (emphasis added). The Commission specifically rejected the requests of two commenters that “the general ‘referenced contract’ definition that applies to futures and options on futures also apply to swaps.” *Id.*

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*; see also *id.* at 3417. In a May 14, 2020 letter, one commenter acknowledged that “the Commission[‘s] . . . proposed definition is narrow to prevent parties with large positions in referenced futures contracts from entering into swaps . . . to net down their overall position for limit purposes,” but nevertheless asked the Commission to define economically equivalent swap to include “economically and *substantively alike* contracts,” *i.e.*, “a closely related swap with the same economic risk profile.” *Id.* at 3301 n.480 (emphasis added).

positions in the futures market.”<sup>20</sup> The narrow definition precludes market participants from structuring “tangentially-related (*i.e.*, non-identical) swaps” so they can “net down large, speculative positions in excess of Federal position limits on futures or options on futures.”<sup>21</sup> The Commission also explained that the narrow definition focuses on “those swaps [*i.e.*, swaps with identical contractual terms and similar delivery dates to futures contracts] that pose the greatest threat for facilitating corners and squeezes.”<sup>22</sup> Finally, the Commission emphasized that the narrow definition of economically equivalent swap “helps prevent regulatory arbitrage as required by CEA section 4a(a)(2)(C) and additionally will strengthen international comity.”<sup>23</sup> It supported this conclusion by citing the similarity of the narrow definition to “the EU definition for OTC contracts that are ‘economically equivalent’ to commodity derivatives traded on an EU trading venue.”<sup>24</sup> And, referring back to its concerns about netting of speculative positions, the Commission observed that “[b]oth the Commission’s definition and the applicable EU regulation are intended to prevent harmful netting.”<sup>25</sup>

In addition to being consistent with the statutory purpose of position limits, preventing regulatory arbitrage and precluding netting, the Commission emphasized that its intentionally narrow definition of economically equivalent swap has the added public policy benefit of minimizing the compliance and implementation burden on market participants.<sup>26</sup> The narrow definition also benefits market integrity by enabling “exchanges, market participants, and the Commission to focus resources on those swaps that pose the greatest threat for facilitating corners and squeezes—that is, those swaps with substantially identical delivery dates and identical material economic terms to futures and options on futures subject to Federal position limits.”<sup>27</sup> Furthermore, the narrow definition should benefit market liquidity “by being, in general, less disruptive to the swaps markets, which in turn may reduce the potential for disruption for the price discovery function compared to a possible alternative, broader definition” and by “reduc[ing] incentives for liquidity providers to move to foreign jurisdictions.”<sup>28</sup> In sum, the Commission’s decision to adopt a narrow definition was careful, detailed, thoughtful and based upon clearly articulated interpretations of the statute and Congress’s and the Commission’s policy objectives. It also was based upon thorough consideration of alternative arguments that

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<sup>20</sup> *Id.* at 3289.

<sup>21</sup> *Id.* at 3290. In the same regard, the CFTC explained that “a more inclusive ‘economically equivalent’ definition that would encompass additional swaps (*e.g.*, swaps that may differ in their ‘material’ terms or physically-settled swaps with delivery dates that diverge by one day or more) could make it easier for market participants to inappropriately net down against their referenced futures contracts by allowing market participants to structure swaps that do not necessarily offer identical risk or economic exposure or sensitivity as the linked futures contract, but which could still be netted under the Final Rules.” *Id.* at 3414.

<sup>22</sup> *Id.* at 3290.

<sup>23</sup> *Id.*

<sup>24</sup> *Id.* at 3290 & n.402.

<sup>25</sup> *Id.* at 3290 n.402.

<sup>26</sup> *Id.* at 3414.

<sup>27</sup> *Id.*

<sup>28</sup> *Id.* at 3415-16.



were advanced during the comment process. The Commission’s statement of agency purpose is entitled to substantial deference by the courts and certainly by the agency itself.

**C. A Swap Must Have Material Contractual Specifications, Terms and Conditions That are Identical to Those of the Particular Referenced Futures Contract Specified in the Swap to be Economically Equivalent**

Regulation 150.1 defines “[e]conomically equivalent swap” as “with respect to a *particular referenced contract*, any swap that has *identical material contractual specifications, terms, and conditions to such referenced contract.*” (Emphasis added). By its express terms, the definition requires a comparison between the “contractual” terms, not the economic terms, of a swap and a “particular” referenced contract. Accordingly, based upon the plain language of the definition, in order to determine whether a swap is an economically equivalent swap, the material contractual terms of the swap must be compared with, and identical to, one specific referenced contract, not to “any” referenced contract, as we understand DMO Staff’s position. As explained below, the specific referenced contract must be the one agreed to by the parties to the swap—the definition refers to “material *contractual* specifications, terms, and conditions”—and identified in the Commodity Reference Price term of the swap. Adopting a broader definition would require disregarding the material contractual terms agreed between the parties.

The Commission identified the contractual terms that are material terms in the preamble to the Position Limits Rule. Material contractual specifications, terms, and conditions “are limited to those provisions that drive the economic value of a swap, including with respect to pricing and risk.”<sup>29</sup> According to the Commission, the material provisions of a swap “include, for example: [t]he **underlying commodity**, including **commodity reference price and grade differentials; maturity or termination dates; settlement type** (*i.e.*, cash-settled versus physically-settled); and, as applicable **for physically delivered swaps, delivery specifications**, including commodity quality standards and delivery locations.”<sup>30</sup> In addition, the Commission explained that “a swap that either *references another referenced contract, or incorporates by reference the other referenced contract’s terms*, is deemed to share identical terms with the referenced contract and therefore qualifies as an economically equivalent swap.”<sup>31</sup> In such a case, the comparison must be between the material terms of the swap and the material terms of the particular referenced contract incorporated by reference in the confirmation, not “any” referenced contract. To the extent that a swap is deemed economically equivalent, the Commission noted that “[a]ny change in the material terms of such swap, however, could render the swap no longer economically equivalent for Federal position limits purposes.”<sup>32</sup>

Importantly, the Commission emphasized that “[b]ecause the Commission considers settlement type to be a material ‘contractual specification, term, or condition,’ *a cash-settled swap could only be deemed to be economically equivalent to a cash-settled referenced*

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<sup>29</sup> *Id.* at 3291.

<sup>30</sup> *Id.* (emphasis added).

<sup>31</sup> *Id.* (emphasis added).

<sup>32</sup> *Id.*

*contract. . . .*<sup>33</sup> This means that a financially-settled swap that specifies a core referenced futures contract as its Commodity Reference Price cannot be economically equivalent to that core referenced futures contract because the latter is physically-settled.

As directed by the rule text and the Commission’s statements in the preamble, the Working Group and outside counsel did not consider terms that are unique to swaps in making their reasonable, good faith determination concerning the regulatory characterization of the swaps listed in Appendix A.<sup>34</sup>

#### **IV. The Commission Should Determine that the Swaps in Appendix A are Not Economically Equivalent Swaps**

For the reasons set forth below, the Associations respectfully request that the Commission determine that the swaps listed in Appendix A are not economically equivalent swaps.

##### **A. The Working Group Memorandum Sets Forth A Detailed Facts and Circumstances Analysis of the Swaps in Appendix A**

Most commodity swaps are documented under an ISDA Master Agreement, a Schedule and a Confirmation. They also incorporate terms defined in the 2005 ISDA Commodity Definitions. Some swaps are documented in bespoke agreements. Because the rule text and preamble of the Position Limits Rule requires a comparison of the contractual terms of a swap and a particular referenced contract, outside counsel and the Working Group examined the

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<sup>33</sup> *Id.* (emphasis added). In the preamble, the Commission explained that “when [it] refers to ‘physically-settled swaps’ for the purpose of [the definition of economically equivalent swap], [it] means a ‘swap that allows for physical settlement or delivery.’” *Id.* at 3292. The Commission did not explain why such a “swap” falls within the definition of swap, which excludes contracts that transfer an ownership interest in an asset and contracts for the sale of a nonfinancial commodity that are intended to be physically settled. *See* CEA §§ 1a(47)(A)(iii) and (B)(ii).

<sup>34</sup> Regulation 150.1 identifies contractual specifications, terms, and conditions that are not material and, therefore, do not affect whether a swap is an economically equivalent swap. Subpart (1) of the definition of economically equivalent swap provides that “for the purpose of determining whether a swap is an economically equivalent swap *with respect to a particular referenced contract*, the swap shall not be deemed to lack identical material contractual specifications, terms, and conditions due to different lot size specifications or notional amounts, delivery dates diverging by less than one calendar day, or different post-trade risk management arrangements.” (Emphasis added). Subpart (2) of the definition provides that “[w]ith respect to any natural gas referenced contract, for the purpose of determining whether a swap is an economically equivalent swap to *such referenced contract*, the swap shall not be deemed to lack identical material contractual specifications, terms, and conditions due to different lot size specifications or notional amounts, delivery dates diverging by less than two calendar days, or different post-trade risk management arrangements.” (Emphasis added). Appendix A does not address the “delivery date” divergence issue because the Commission’s discussion of delivery date divergence only appears in the context of so-called “physically delivered swaps.” *See, e.g.*, Position Limits Rule, 86 Fed. Reg. at 3291-94, 3296. The Working Group did not provide outside counsel with any examples of a physically-delivered swap. In the preamble, the CFTC explained that terms that are “unique to swaps” are immaterial. *Id.* at 3291. Consequently, the following terms and conditions are not material when determining whether a swap is an economically equivalent swap: clearing arrangements, governing law, designating business day or holiday conventions; day count; calculation agent; dispute resolution mechanisms; choice of law; or representations and warranties. *Id.*

contractual terms of each swap in Appendix A and the contractual terms of the particular referenced futures contract specified by the parties in the swap agreement.

### **1. Material Commodity Swap Contractual Terms**

A typical commodity swap confirmation includes the contractual terms identified in **Appendix B**. Based upon the CFTC's explanation in the preamble, the most important material contractual terms are the Effective date, Termination Date, Commodity, Settlement method, and Commodity Reference Price.<sup>35</sup>

### **2. Material Referenced Futures Contract Contractual Terms**

A typical commodity futures contract includes the contractual specifications listed by the relevant DCM. As examples, we have attached the contract specifications of the NYMEX HENRY HUB NATURAL GAS FUTURES, the NYMEX NATURAL GAS (HENRY HUB) LAST-DAY FINANCIAL FUTURES and ICE Henry LD1 Fixed Price Future, as **Appendices D, E and F**, respectively. Based upon the CFTC's guidance, the most important material contractual terms of a commodity futures contract are the Commodity, Listed Contracts, Settlement Method, Floating Price or Reference Price, and Termination of Trading.<sup>36</sup>

## **B. Analysis of Sample Confirmations**

For purposes of outside counsel's and the Working Group's analysis, the most relevant material contractual terms of a swap are the commodity reference price, the underlying commodity, the settlement type (physical or financial) and the term or duration of the contract. These are the terms identified by the Commission and are clearly those that determine the value of a swap. As a result, they are the appropriate terms on which to rely in identifying economically equivalent swaps. As noted above, a summary table of outside counsel's analysis is set forth in Appendix A.

### **1. Commodity / Commodity Reference Price and Settlement Type**

The commodity type material term is reasonably self-explanatory provided that the comparison between a swap and a particular reference contract takes into account any specified grade differentials. The Commodity Reference Price of most of the Working Group swap confirmations incorporated commodity reference prices defined in the 2005 ISDA Commodity Definitions. For example, in natural gas, certain swaps referenced "Natural Gas – Henry Hub – NYMEX," which is defined in Section 7.1, Sub-Annex A, of the 2005 ISDA Commodity Definitions.

Because the Commodity Reference Price in a swap points to a particular referenced futures contract, in order to determine whether the swap is an economically equivalent swap, the material contractual terms of the swap must be compared to the material contractual terms of the

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<sup>35</sup> Capitalized terms have the meaning given them in the 2005 ISDA Commodity Definitions.

<sup>36</sup> Capitalized terms have the meaning given them in the relevant DCM futures contract specifications.

particular referenced futures contract. Comparing the material contractual terms of the swap with those of any other referenced futures contract, would be inconsistent with the Commission's statement in the preamble that the Commodity Reference Price is one of the "material" provisions of a swap that drives its economic value and, therefore, is key to the analysis of whether a particular swap is an economically equivalent swap.<sup>37</sup>

If the Commodity Reference Price of a swap is "Natural Gas – Henry Hub – NYMEX", a market participant must compare the material contractual terms of the swap to the material contract specifications of the NYMEX HENRY HUB NATURAL GAS FUTURES contract, *i.e.*, the particular referenced futures contract that drives the economic value of the swap.<sup>38</sup> The material contractual terms of the NYMEX HENRY HUB NATURAL GAS FUTURES contract include commodity (natural gas), settlement method (deliverable) and term (monthly terminating on the 3<sup>rd</sup> last business day of the month prior to the contract month). If any of the material contract terms of the swap and the referenced futures contract are not identical, the swap is not an economically equivalent swap. In this example, the settlement types of the swap (financial) and the referenced futures contract (physical) are not identical. Accordingly, the financially-settled swap is not economically equivalent to the physically-settled referenced futures contract. For the same reason, the financially-settled swaps in Appendix A that point in the Commodity Reference Price to a particular physically-settled referenced futures contract should not be characterized as economically equivalent swaps.

## 2. Term or Duration

DCMs list futures contracts with identified settlement periods that expire at a specific point in time specified in the contract specifications. In order to be economically equivalent, a swap must have a term that is identical to the term of the referenced futures contract specified in the Commodity Reference Price. The only swaps that have a term that is the same as a referenced futures contract are so called-bullet swaps that settle based upon the final settlement price of a single futures contract. To the extent that the term or duration of a swap has a term or duration that exceeds the term of a single futures contract, the term or duration of the swap is not identical to a referenced futures contract. Thus, even if all other material terms of a swap are identical to those of a particular referenced futures contract, if the duration of the swap and the duration of the referenced futures contract differ, the swap is not an economically equivalent swap.

As shown in Appendix A, in addition to having different settlement types, most of the swaps provided to outside counsel by the Working Group have different durations than the particular referenced futures contract specified in the Commodity Reference price. For this independent reason, the Commission should determine that those swaps are not economically equivalent swaps.

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<sup>37</sup> Position Limits Rule, 86 Fed. Reg. at 3291.

<sup>38</sup> See **Appendix C**.

### **C. Economically Equivalent Swap Example**

Although not included among the swaps analyzed in Appendix A, if a financially-settled swap specified as its Commodity Reference Price the price of a financially-settled futures contract (e.g., the ICE Futures U.S. Henry LD1 Fixed Price Future—see the contract specifications in **Appendix E**), the swap would be an economically equivalent swap provided that all other material contractual terms are identical. In this regard, the Commission explained that “a cash-settled swap that either settles to the pricing of a corresponding cash-settled referenced contract, or incorporates by reference the terms of such referenced contract, would be deemed to be economically equivalent to the referenced contract.”<sup>39</sup> To illustrate, FIA has attached as **Appendix F** a hypothetical swap that uses as its Commodity Reference Price “NYMEX NATURAL GAS (HENRY HUB) LAST-DAY FINANCIAL FUTURES” with a term of March 29 – March 29, 2023. In this example, the commodity, Commodity Reference Price, settlement type and term of the swap and the referenced futures contract are identical. Hence, the swap would qualify as an economically equivalent swap.

### **V. DMO’s Informal Position Creates Uncertainty About How to Apply the Definition of Economically Equivalent Swap**

DMO’s informal position that a swap that specifies as its Commodity Reference Price a physically settled core referenced contract is economically equivalent to “any” look-a-like financially-settled referenced futures contract is not supported by the text of the definition of economically equivalent swap in the Position Limits Rule. It also conflicts with the Commission’s explanations in the preamble concerning how to apply the definition and the associated position limits. Because DMO’s informal position is inconsistent with the Commission’s clear statement of its intent, it has the effect of undermining the Commission’s stated policy objectives, discussed above, for its adoption of the Position Limits Rule.

The portion of DMO’s informal position that is consistent with the regulatory definition, the preamble and the Working Group’s reasonable, good faith determination is the statement that “the financially-settled swap is not deemed to be an EE swap to the physically-settled core referenced futures contract. . . .” That conclusion is correct for two reasons: (1) the Commodity Reference Price “material contractual . . . term[]” specified by the parties to the swap is the core referenced futures contract, *i.e.*, the “particular” referenced contract; and (2) the settlement types—financial *v.* physical—of the two contracts are not identical.

#### **A. DMO’s Informal Communication Does Not Provide a Framework for Determining Whether a Swap is an Equivalent Swap**

The text of the definition of economically equivalent swap requires a determination of whether the material contractual terms of a swap and a particular referenced contract are “identical.” If any of the material terms of the two contracts are not identical, the swap is not an economically equivalent swap. Instead of focusing on whether the contractual terms of the swap

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<sup>39</sup> Position Limits Rule, 86 Fed. Reg. at 3291 n.405.

and the particular referenced futures contract specified in the Commodity Reference Price are identical, DMO appears to focus on whether the price terms of a swap and “any” look-a-like financially-settled referenced futures contract “mirror” one another. The concept of a price “mirror” does not appear in the definition of economically equivalent swap or in the preamble and is inconsistent with the Commission’s explanation about how to apply the definition of economically equivalent swap. Furthermore, DMO’s informal communication did not address how the rule text or the preamble led DMO to draw a different conclusion from the Working Group’s facts and circumstances analysis.

### **1. DMO’s Informal Position Does Not Treat Commodity Reference Price as a Material Contract Term of a Swap**

Although DMO’s informal communication mentions the Commodity Reference Price term, it does not treat the Commodity Reference Price specified in the swap as a material contractual term as required by the definition of economically equivalent swap. Where the parties to a swap contract specify as the Commodity Reference Price a physically-settled referenced futures contract, the Commodity Reference Price is *not* identical to a particular financially-settled referenced futures contract and, thus, the swap is *not* economically equivalent to the financially-settled referenced futures contract. By suggesting that a swap with a physically-settled referenced futures contract as the Commodity Reference Price is economically equivalent to a financially-settled look-a-like referenced futures contract, DMO’s informal communication effectively nullifies Commodity Reference Price as a material contractual term of the swap. For example, DMO did not explain how two swaps with non-identical Commodity Reference Price material contract terms—one specifying a physically-settled core referenced futures contract and the other specifying a financially-settled referenced futures contract—could be contractually identical to the same referenced futures contract. If the Commodity Reference Price is a material contractual term that must be identical to a Referenced Contract, swaps with a different Commodity Reference Price cannot be identical to the same referenced contract.

Furthermore, by pointing to “any” look-a-like financially-settled referenced futures contract rather than the physically-settled core referenced futures contract specified in the Commodity Reference Price agreed by the parties, DMO’s informal position effectively changes a material contractual term of the swap without the consent of the parties.<sup>40</sup>

Based upon the plain text of the definition of economically equivalent swap and the preamble, in order for a financially-settled swap to have material contract terms that are identical to those of a referenced futures contract, the swap must specify as its Commodity Reference Price a particular financially-settled look-a-like referenced futures contract. Only if a swap uses the price of such a look-a-like referenced futures contract as its Commodity Reference Price, is it

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<sup>40</sup> Under New York law, to be enforceable the modification of a contract must be agreed to by the parties. *Dallas Aerospace, Inc. v. CIS Air Corp.*, 352 F.3d 775, 783 (2d Cir. 2003); *see also Beacon Terminal Corp. v. Chemprene, Inc.*, 75 A.D.2d 350, 354 (N.Y. App. Div. (1980) (“Fundamental to the establishment of a contract modification is proof of each element requisite to the formulation of a contract, including mutual assent [by the parties] to its terms.”)).

possible that the swap may be an economically equivalent swap (all other material terms being identical).

The following example illustrates one reason why a swap that uses as its Commodity Reference Price a physically-settled referenced futures contract should not be interpreted as economically equivalent to a financially-settled look-alike referenced futures contract. Assume that a bullet swap names the NYMEX physically-settled natural gas futures contract, NG, as its Commodity Reference Price.<sup>41</sup> NG is a Core Reference Futures Contract. The settlement of the bullet swap is calculated based upon the closing price on the last trading day of the spot month. ICE lists a financially-settled natural gas futures contract, LD1, the specifications of which include NG as its Reference Price.<sup>42</sup> Assume that the NG contract on the last trading day for the spot month closes at \$6.00 per MMBtu. According to its specifications, the LD1 contract also would settle at \$6.00. Now assume that, due to some extraneous event, the underlying cash price for natural gas at Henry Hub is quoted by some market participants at prices between \$6.05 and \$6.10 / MMBtu. CME nevertheless allows the \$6.00 settlement of the NG contract to stand. ICE, however, acting pursuant to its recently amended Rule 4.34, revises the final settlement price of the LD1 contract to \$6.05 on the grounds that LD1's Settlement Price was erroneous. Based upon the material contractual terms of the swap, the settlement of the swap will be calculated based upon the NG contract settlement of \$6.00. Contrary to DMO's informal position, as between the parties to the swap, it is the material specifications, terms and conditions of the NG contract, not those of the LD1 contract, that in the Commission's words "drive the economic value of a swap."<sup>43</sup>

## **2. DMO's Informal Position Does Not Address Settlement Type as a Material Contract Term of a Swap**

DMO's informal view does not consider the settlement type—another Commission-identified material contract term—of the swap and the particular referenced contract specified in the swap. Contrary to the plain text of the definition and the Commission's statements in the preamble, DMO concludes that a financially-settled swap that specifies as its Commodity Reference Price a physically-settled futures contract is an economically equivalent swap. But a swap that includes a Commodity Reference Price based upon the price of a physically-settled referenced futures contract is not an economically equivalent swap because the settlement type of the swap (financial) is not identical to the settlement type of the particular physically-settled referenced futures contract (physical) specified in the swap.

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<sup>41</sup> See Appendix B.

<sup>42</sup> See Appendix D.

<sup>43</sup> Position Limits Rule, 86 Fed. Reg. at 3291.

**B. DMO’s Informal Position Would Have Several Consequences That Are Inconsistent with the Commission’s Stated Intent in the Preamble**

**1. Substantial Expansion of Swaps that Can be Netted Against Futures Contracts**

DMO’s informal position, if adopted, would open the door to the type of netting of referenced contracts that the Commission explicitly sought to preclude through its intentionally narrow definition of economically equivalent swap. Under the Commission’s explanation in the preamble and the Working Group’s reasonable, good faith determination, only a limited number of economically equivalent swaps would be eligible to be netted against look-a-like financially-settled referenced futures contracts. Under DMO’s informal position, many bullet swaps that use as their Commodity Reference Price a physically-settled core referenced futures contract will be eligible to net against any financially-settled look-a-like referenced futures contract with the same underlying commodity. Then, contrary to the Commission’s express intent, market participants will be able to acquire large financially-settled referenced futures contract positions, which, because they will net against offsetting swap positions, will result in a flat position thereby limiting the effectiveness of federal position limits.

**2. More Incentive to Engage in Regulatory Arbitrage**

As discussed above, one of the Commission’s goals in promulgating a narrow definition of economically equivalent swap was to align it with “the EU definition for OTC contracts that are ‘economically equivalent’ to commodity derivatives traded on an EU trading venue.”<sup>44</sup> According to the Commission, aligning the two definitions “helps prevent regulatory arbitrage as required by CEA section 4a(a)(2)(C) and additionally will strengthen international comity.”<sup>45</sup> Under DMO’s informal view, market participants and their affiliates that transact in the U.S. and the EU may be able to choose where they book swap positions depending upon whether a broad (DMO informal position) or narrow (EU definition) definition of economically equivalent swap benefits their particular portfolio of derivative transactions.<sup>46</sup>

**3. Equating the Definition of Economically Equivalent Swap with the Definition of Referenced Contract without Public Notice and Comment**

The mirror concept on which DMO’s informal position is based is a proxy for price linkage. The definition of referenced contract includes, among other contracts, “a futures contract or an option on a futures contract . . . that is . . . [*d*]irectly or indirectly linked, including being partially or fully settled on, or priced at a fixed differential to, the price of [*a*] particular

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<sup>44</sup> *Id.* at 3290 & n.402.

<sup>45</sup> *Id.* at 3290.

<sup>46</sup> The Associations also note that the Commission has not yet proposed for public comment cross-border rules regarding the application of position limits to economically equivalent swaps. The Commission would benefit from public comment about the unintended consequences of a broad interpretation of the definition of economically equivalent swap, including the impact on cross-border regulation of such swaps.



*core referenced futures contract.*” (Emphasis added). Characterizing a swap as economically equivalent when it specifies a physically-settled core referenced futures contract as its Commodity Reference Price based upon DMO’s “mirror” concept would substantively amend the definition of economically equivalent swap to be the same as the definition of referenced futures contract. Just like the definition of referenced contract, DMO’s informal view focuses on the price linkage—the so-called “mirror”—between the swap and the futures contract rather than on whether the material contract terms of the two contracts are the same. Furthermore, it is inconsistent with the Commission’s considered decision to adopt a definition of economically equivalent swap that is narrower than the definition of referenced futures contract.<sup>47</sup>

#### 4. Greater Compliance Burden on Market Participants

As explained above, the Commission emphasized in the preamble to the Position Limits Rule that its intentionally narrow definition of economically equivalent swap has the important public policy benefit of minimizing the compliance and implementation burden on market participants.<sup>48</sup> DMO’s informal position has the opposite effect because it does not appear to be premised on the rule text or the preamble, and does not provide objective metrics for determining whether a swap that points to a particular referenced futures contract is an economically equivalent swap.

The Commission and the exchanges treat position limits violations as strict liability offenses.<sup>49</sup> Consequently, monitoring economically equivalent swaps for compliance with applicable position limits is critically important to members of the Associations and all market participants. Some Commission registrants have affirmative regulatory obligations to address compliance with position limits. For example, Regulation 23.601 requires swap dealers to establish written policies and procedures, provide training, supervise and test their ability to comply with position limits, including those applicable to economically equivalent swaps. Similarly, exchanges expect clearing members to discover and liquidate the excess positions (above limits) of their customers within a reasonable period of time, typically within one business day.<sup>50</sup>

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<sup>47</sup> *Id.* at 3289. During our meeting on July 13, 2022, DMO Staff asked the following question:

- If  $A = B$  (A is the physically-settled futures contract, and B is the cash-settled referenced contract); and
- $B = C$  (B is the cash-settled referenced contract, and C is a swap that is economically equivalent to B); then
- Why does  $C \neq A$  (C is a swap and A is the physically-settled futures contract)?

The reason why C does not equal A is because the methodology in the definition of referenced contract used to compare A and B (price linkage) is not the same as the methodology in the definition of economically equivalent swap used to compare C to either A or B (whether the material contract terms are identical).

<sup>48</sup> *Id.* at 3414.

<sup>49</sup> *See, e.g., Saberi v. CFTC*, 488 F.3d 1207, 1212 n.4 (9th Cir. 2007) (citing *CFTC v. Hunt*, 591 F.2d 1211, 1218 (7th Cir. 1979)).

<sup>50</sup> *See, e.g.,* Market Regulation Advisory Notice, CME Group RA2205-5, at 8 (Q&A15) (Sept. 23, 2022), <https://www.cmegroup.com/rulebook/files/cme-group-Rule-562.pdf>; ICE Futures U.S., Inc. Rule 6.13(a)(vi) and (b), [https://www.ice.com/publicdocs/rulebooks/futures\\_us/6\\_Regulatory.pdf](https://www.ice.com/publicdocs/rulebooks/futures_us/6_Regulatory.pdf).

DMO's informal position would impose substantial compliance and implementation burdens on market participants. Market participants that transact swaps in the U.S. and the E.U. would have to design or modify systems to identify and monitor swap positions based upon inconsistent definitions of economically equivalent swap. For swaps subject to federal position limits, information technology and operations systems would need to be reconfigured to identify a much broader class of economically equivalent swaps. Doing so intraday for OTC swap positions will be more challenging under DMO's broad view of the scope of the definition. In addition, new systems would need to be designed and programmed to identify, match and net economically equivalent swaps against opposite referenced futures contract positions. The netted positions then must be monitored for compliance with applicable position limits.

**VI. If the Commission Determines that Any of the Swaps Listed in Appendix A are Economically Equivalent Swaps, it Should Stay the Compliance Date for Any Such Swaps Until 12 Months After it Makes Such a Determination**

The current position limits compliance date for economically equivalent swaps is January 1, 2023. Up to now, members of the Associations have been developing information technology and operations systems designed to monitor economically equivalent swap positions for compliance with position limits based upon the Working Group's reasonable good faith determination. Members of the Associations are prepared to comply with the current effective date for any swaps that they have reasonably and in good faith determined to be economically equivalent swaps.

If, however, the Commission determines that any of the swaps listed in Appendix A are economically equivalent swaps, members of the Associations and other market participants will need a commercially reasonable period to modify all of their information technology, operations and compliance systems, policies and procedures. The commercially reasonable period should take into account the information technology blackout period that most publicly traded companies impose near year-end to avoid the errors that new and untested systems could create in their year-end financial statements. Based upon the complexity of the systems and programming required to identify, net and monitor economically equivalent swaps under a new and broader definition than the one in the Position Limits Rule, members of the Associations estimate that they will need at least 12 months to come into compliance. Accordingly, FIA requests that the Commission extend the position limits compliance date for any swaps that it determines to be economically equivalent swaps in response to this petition to a date that is no earlier than 12 months after the date of such a determination. In granting any such extension, the Associations request that the Commission take into account the year-end information technology blackouts imposed by publicly traded companies when setting the new compliance date.

## VII. Conclusion

For the foregoing reasons, the Associations respectfully request that the Commission provide market participants with regulatory certainty by determining that the swaps listed in Appendix A are not economically equivalent swaps. Furthermore, if the Commission determines that any of the swaps in Appendix A are economically equivalent swaps, the Associations requests that the Commission extend the position limits compliance date for any such swaps to a date that is no earlier than 12 months after the date of such a determination.

Respectfully submitted,



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Allison P. Lurton  
Chief Legal Officer & General Counsel  
Futures Industry Association



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Steven Kennedy  
Global Head of Public Policy  
ISDA

Attachment

cc: Rostin Behnam, Chairman  
Kristin N. Johnson, Commissioner  
Christy Goldsmith Romero, Commissioner  
Summer K. Mersinger, Commissioner  
Caroline D. Pham, Commissioner  
Vincent McGonagle, Director, Division of Market Oversight  
Robert Schwartz, General Counsel  
Michael Sorrell, FIA  
Christopher Young, ISDA

# **EXHIBIT 1**

**July 14, 2022**

## **Working Group Memorandum and Appendices**

- A** Analysis of Sample Swaps
- B** Commodity swap confirmation
- C** NYMEX HENRY HUB NATURAL GAS FUTURES contract specifications
- D** NYMEX NATURAL GAS (HENRY HUB) LAST-DAY FINANCIAL FUTURES contract specifications
- E** ICE Henry LD1 Fixed Price Future contract specifications
- F** Hypothetical swap that uses as its Commodity Reference Price “NYMEX NATURAL GAS (HENRY HUB) LAST-DAY FINANCIAL FUTURES” with a term of March 29 – March 29, 2023

*Confidential*

**To:** The Futures Industry Association Inc.

**From:** Paul J. Pantano, Jr.  
Neal E. Kumar

**Date:** July 1, 2022 (Revised July 14, 2022)

**Re:** Economically Equivalent Swaps

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## I. Introduction

The Futures Industry Association (“**FIA**”) requested that Willkie Farr & Gallagher LLP (“**Willkie**”) prepare a legal and factual analysis of the scope of the definition of “economically equivalent swap” under the U.S. Commodity Futures Trading Commission’s (“**CFTC**” or “**Commission**”) final rule imposing speculative position limits on derivatives (“**Position Limits Rule**”).<sup>1</sup> Since publication of the Position Limits Rule, FIA has held regular meetings with members of its Position Limits Working Group (“**Working Group**”) to assist firms in complying with the Position Limits Rule. As part of that effort, firms have raised a number of interpretive questions and topics relating to the Position Limits Rule and its adopting release.

One of the topics raised in the Working Group is the scope of swaps that fall within the definition of economically equivalent swap in CFTC Rule 150.1, 17 C.F.R. 150.1. Swaps that fall within the definition will be subject to federal position limits as of January 1, 2023. Based upon the number and similarity of the questions raised by members of the Working Group regarding the scope of the definition, FIA asked Willkie to prepare a memorandum and the accompanying table attached hereto as **Appendix A** as a reference for firms that are analyzing their swaps portfolios in preparation for complying with the new federal limits that will apply to economically equivalent swaps. This memorandum summarizes Willkie’s analysis of whether there is a reasonable basis to conclude that the swaps set forth in Appendix A are, or are not, economically equivalent swaps.<sup>2</sup>

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<sup>1</sup> *Position Limits for Derivatives*, 86 Fed Reg. 3236 (Jan. 14, 2021).

<sup>2</sup> During a call on Friday, June 17, 2022, after we had completed the analysis described in, but before we had finalized, this Memorandum, a member of the Staff of the Division of Market Oversight (“**DMO**”) informed FIA that some DMO Staff may be of the view that a financially-settled swap can have material contractual terms that are identical to the material contractual terms of the particular physically-settled referenced futures contract specified in the Commodity Reference Price of the swap. We discussed this issue with Staff during a meeting on July 13, 2022. For all of the reasons discussed herein, we believe that treating a financially-settled swap as having identical material contract terms as a physically-settled referenced futures contract would be inconsistent with (1) the plain text of the Position Limits Rule, (2) the Commission’s stated intent and purpose of the rule as described throughout the pages of the preamble cited herein, and (3) the material contractual terms agreed between the parties to the swaps listed in Appendix A.

## II. Legal Analysis

### A. Methodology

The CFTC explained in the preamble to the Position Limits Rule that determining whether a swap is economically equivalent to a particular referenced futures contract requires a “a facts and circumstances analysis.”<sup>3</sup> For this reason, and because “most physical commodity swaps are created bilaterally between counterparties and traded” in the over-the-counter (“OTC”) market, the CFTC declined to publish a list of swaps that are economically equivalent to referenced futures contracts.<sup>4</sup> The Commission emphasized that it “believes that market participants are best positioned to determine whether particular swaps share identical material terms with referenced contracts and would therefore qualify as ‘economically equivalent’ for purposes of Federal position limits.”<sup>5</sup> Consequently, the CFTC provided market participants with the discretion to determine whether a swap is economically equivalent to a referenced futures contract as long as they perform reasonable due diligence and make equivalence determinations in good faith.

In accordance with the Commission’s guidance, we conducted a three-part analysis in preparing this memorandum. First, we reviewed the plain text of the Position Limits Rule and the CFTC’s explanation of the rule in the preamble to the rule. Second, we reviewed sample swap agreement confirmations across several commodity asset classes provided to us by members of the Working Group. The confirmations were redacted to remove counterparty identifying information, but otherwise contain all of the material terms of the swap. Third, we compared the material contractual specifications, terms, and conditions of the swaps to the material contractual specifications, terms, and conditions of the particular referenced futures contract specified in the swap to determine whether they were identical. Based upon this determination, we reached conclusions about whether the swaps listed in Appendix A reasonably and in good faith can be characterized as economically equivalent or non-equivalent swaps.

### B. The Plain Text of the Rule and CFTC Guidance

#### 1. Interpreting An Agency Rule

The Supreme Court has held that, when interpreting federal agency regulations, “courts must carefully consider the text, structure, history and purpose of a regulation. . . .”<sup>6</sup> As a prerequisite to the validity of regulations, the Administrative Procedure Act requires every agency, including the CFTC, to “incorporate in the rules adopted a concise general statement of their basis and purpose,” *i.e.*, the preamble to the rule.<sup>7</sup> The basis and purpose of a regulation

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<sup>3</sup> *Id.* at 3295.

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

<sup>6</sup> *Kisor v. Wilkie*, 580 U.S. \_\_\_, 139 S. Ct. 2400, 2415 (2019). *See also Dresser-Rand Co. v. Petroleos de Venezuela, S.A.*, No. 19 CIV. 2689 (LLS), 2021 WL 5831766 at \*6 (S.D.N.Y. Dec. 8, 2021). Only if a regulation is ambiguous should a court conduct an independent analysis of whether an agency’s interpretation of its own regulation is reasonable and entitled to controlling weight. *Kisor*, 139 S. Ct. at 2415.

<sup>7</sup> 5 U.S.C. § 553(c). In the CFTC’s statement of the “basis and purpose” of the definition of economically equivalent swap, it noted that because the CEA “does not define the term ‘economically equivalent,’ the Commission is applying its expertise in construing such term consistent with the policy goals articulated by Congress, including in CEA sections 4a(a)(2)(C) and 4a(a)(3) . . . .” 86 Fed. Reg. at 3413.

can be “discerned from the regulation’s text and accompanying explanatory material. . . .”<sup>8</sup> The Second Circuit similarly has explained that regulatory interpretation requires an “examin[ation] [of] the regulation’s text in light of its purpose, as stated in the regulation’s preamble.”<sup>9</sup>

We applied this approach—examining the text and structure of the Position Limits Rule and its purpose as reflected in the preamble—in assessing the scope of the definition of economically equivalent swap. In our view, the definition is not ambiguous. But even assuming for the sake of argument that it is, we believe that our interpretation is reasonable and that a contrary interpretation is not supported by either the text and structure of the definition or the guidance provided by the Commission in the preamble. This is particularly true in light of the CFTC’s explanation that the express purpose of the definition is to apply only to a narrow class of swaps.

## 2. The CFTC Intentionally Adopted a Narrow Definition of Economically Equivalent Swap

The CFTC stated unequivocally in the preamble that it intentionally adopted a narrow definition of economically equivalent swap.<sup>10</sup> Based upon a careful review of the statutory framework for setting of federal speculative position limits, the CFTC explained that “Congress’s underlying policy goals in CEA section 4a(a)(2)(C) and (3)(B) are best achieved by *adopting a narrow definition of ‘economically equivalent swap,’* compared to the broader definition of ‘referenced contract.’”<sup>11</sup> According to the CFTC, “the relatively narrow definition supports the statutory objective in CEA section 4a(a)(2)(C) by not causing price discovery to shift to trading in foreign markets.”<sup>12</sup> Furthermore, the narrow definition of economically equivalent swap “supports the statutory objectives in CEA section 4a(a)(3)(B)(i) and (ii) by helping to prevent excessive speculation and market manipulation, including corners and squeezes, respectively, by: (1) focusing on swaps that are the most economically equivalent in every significant way to the futures contracts and options on futures contracts for which the Commission deems position limits to be necessary; and (2) limiting the ability of speculators to obtain excessive positions through netting.”<sup>13</sup>

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<sup>8</sup> Edgar and Stack, *The Authority and Interpretation of Regulations*, Modern Law Review, Vol. 82, Issue 6 (November 2019), at 1010.

<sup>9</sup> *Halo v Yale Health Plan*, 819 F.3d 42, 52 (2d Cir. 2016), cited in *The Authority and Interpretation of Regulations*, at 1026.

<sup>10</sup> On October 5, 2020, a few months before the CFTC issued the Final Position Limits Rule, FIA Staff and Willkie discussed the expected final rule with the then Senior Counsel to CFTC Chairman Heath Tarbert. During the call, the Senior Counsel informed FIA that the scope of economically equivalent swaps subject to position limits “should be a very small population.”

<sup>11</sup> Position Limits Rule at 3289 (emphasis added). The Commission specifically rejected the request of CME Group and Better Markets that “the general “referenced contract” definition that applies to futures and options on futures also apply to swaps.” *Id.*

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

The Commission explicitly declined to adopt a broader definition of economically equivalent swap as requested by some commenters.<sup>14</sup> The CFTC’s primary objective in adopting a narrow definition was to prevent “parties from using netting of swaps to create large positions in the futures market.”<sup>15</sup> The narrow definition precludes market participants from structuring “tangentially-related (*i.e.*, non-identical) swaps” so they can “net down large, speculative positions in excess of Federal position limits on futures or options on futures.”<sup>16</sup> The CFTC also justified the narrow definition as focusing on “those swaps [*i.e.*, swaps with identical contractual terms and similar delivery dates to futures contracts] that pose the greatest threat for facilitating corners and squeezes.”<sup>17</sup> Finally, the CFTC emphasized that the narrow definition of economically equivalent swap “helps prevent regulatory arbitrage as required by CEA section 4a(a)(2)(C) and additionally will strengthen international comity.”<sup>18</sup> It supported this conclusion by citing the similarity of the narrow definition to “the EU definition for OTC contracts that are ‘economically equivalent’ to commodity derivatives traded on an EU trading venue.”<sup>19</sup> And, referring back to its concerns about netting of speculative positions, the CFTC observed that “[b]oth the Commission’s definition and the applicable EU regulation are intended to prevent harmful netting.”<sup>20</sup>

In addition to being consistent with the statutory purpose of position limits, preventing regulatory arbitrage and precluding netting, the CFTC emphasized that its intentionally narrow definition of economically equivalent swap has the added public policy benefit of minimizing the compliance and implementation burden on market participants.<sup>21</sup> The narrow definition also benefits market integrity by enabling “exchanges, market participants, and the Commission to focus resources on those swaps that pose the greatest threat for facilitating corners and squeezes—that is, those swaps with substantially identical delivery dates and identical material economic terms to futures and options on futures subject to Federal position limits.”<sup>22</sup> Furthermore, the narrow definition should benefit market liquidity “by being, in general, less disruptive to the swaps markets, which in turn may reduce the potential for disruption for the price discovery function compared to a possible alternative, broader definition” and by “reduc[ing] incentives for liquidity providers to move to foreign jurisdictions.”<sup>23</sup>

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<sup>14</sup> *Id.*; see also *id.* at 3417. In its May 14, 2020 comment letter, the CME Group acknowledged that “the Commission[’s] . . . proposed definition is narrow to prevent parties with large positions in referenced futures contracts from entering into swaps . . . to net down their overall position for limit purposes,” but nevertheless asked the Commission to define economically equivalent swap to include “**economically and substantively alike contracts**,” *i.e.*, “a closely related swap with the same economic risk profile.” Letter at 3 (emphasis added).

<sup>15</sup> *Id.*

<sup>16</sup> *Id.* at 3290. In the same regard, the CFTC explained that “a more inclusive ‘economically equivalent’ definition that would encompass additional swaps (*e.g.*, swaps that may differ in their ‘material’ terms or physically-settled swaps with delivery dates that diverge by one day or more) could make it easier for market participants to inappropriately net down against their referenced futures contracts by allowing market participants to structure swaps that do not necessarily offer identical risk or economic exposure or sensitivity as the linked futures contract, but which could still be netted under the Final Rules.” *Id.* at 3414.

<sup>17</sup> *Id.*

<sup>18</sup> *Id.* at 3290.

<sup>19</sup> *Id.*, n. 402.

<sup>20</sup> *Id.*

<sup>21</sup> *Id.* at 3414.

<sup>22</sup> *Id.*

<sup>23</sup> *Id.* at 3415-16.



### 3. Material Contractual Specifications, Terms and Conditions

Rule 150.1 defines “[e]conomically equivalent swap” as “with respect to a *particular referenced contract*, any swap that has *identical material contractual specifications, terms, and conditions to such referenced contract*.” (Emphasis added). By its express terms, the definition requires a comparison between the “contractual” terms, not the economic terms, of a swap and a “particular” referenced contract. Accordingly, based upon the plain language of the definition, in order to determine whether a swap is an economically equivalent swap, the material contractual terms of the swap must be compared with, and identical to, one specific referenced contract, not to one or more referenced contracts. As explained below, the specific referenced contract must be the one agreed to by the parties to the swap—the definition refers to “material *contractual specifications, terms, and conditions*”—and identified in the Commodity Reference Price term of the swap.

The CFTC provided further guidance concerning which contractual terms are material terms in the preamble to the Position Limits Rule. Material contractual specifications, terms, and conditions “are limited to those provisions that drive the economic value of a swap, including with respect to pricing and risk.”<sup>24</sup> According to the Commission, the material provisions of a swap “include, for example: [t]he **underlying commodity**, including **commodity reference price and grade differentials; maturity or termination dates; settlement type** (*i.e.*, financially-settled versus physically-settled); and, as applicable **for physically delivered swaps, delivery specifications**, including commodity quality standards and delivery locations.”<sup>25</sup> In addition, the Commission explained that “a swap that either *references another referenced contract, or incorporates by reference the other referenced contract’s terms*, is deemed to share identical terms with the referenced contract and therefore qualifies as an economically equivalent swap.”<sup>26</sup> In such a case, the comparison must be between the material terms of the swap and the material terms of the particular referenced contract incorporated by reference. To the extent that a swap is deemed economically equivalent, the CFTC noted that “[a]ny change in the material terms of such swap, however, could render the swap no longer economically equivalent for Federal position limits purposes.”<sup>27</sup>

The CFTC emphasized that “[b]ecause the Commission considers settlement type to be a material ‘contractual specification, term, or condition,’ *a cash-settled swap could only be deemed to be economically equivalent to a cash-settled referenced contract*, and a physically-settled swap could only be deemed to be economically equivalent to a physically-settled referenced contract.”<sup>28</sup> This means that a financially-settled swap cannot be economically equivalent to a Core Referenced Futures Contract, all of which are physically-settled.

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<sup>24</sup> *Id.* at 3291.

<sup>25</sup> *Id.*

<sup>26</sup> *Id.* (emphasis added).

<sup>27</sup> *Id.*

<sup>28</sup> *Id.* In the preamble, the Commission explained that “when [it] refers to ‘physically-settled swaps’ for the purpose of [the definition of economically equivalent swap], [it] means a ‘swap that allows for physical settlement or delivery.’” *Id.* at 3292. The Commission did not explain why such a “swap” falls within the definition of swap, which excludes contracts that transfer an ownership interest in an asset and contracts for the sale of a nonfinancial commodity that are intended to be physically settled. See CEA §§ 1a(47)(A)(iii) and (B)(ii).

#### 4. Immaterial Contractual Specifications, Terms and Conditions

Rule 150.1 also identifies contractual specifications, terms, and conditions that are not material and, therefore, do not affect whether a swap is an economically equivalent swap. Subpart (1) of the definition of economically equivalent swap provides that “for the purpose of determining whether a swap is an economically equivalent swap *with respect to a particular referenced contract*, the swap shall not be deemed to lack identical material contractual specifications, terms, and conditions due to different lot size specifications or notional amounts, delivery dates diverging by less than one calendar day, or different post-trade risk management arrangements.” (Emphasis added). Subpart (2) of the definition provides that “[w]ith respect to any natural gas referenced contract, for the purpose of determining whether a swap is an economically equivalent swap to *such referenced contract*, the swap shall not be deemed to lack identical material contractual specifications, terms, and conditions due to different lot size specifications or notional amounts, delivery dates diverging by less than two calendar days, or different post-trade risk management arrangements.” (Emphasis added).<sup>29</sup> Importantly for purposes of making a good faith determination of whether a swap is economically equivalent to a particular referenced contract, and as discussed further below, subpart (3) of the definition provides that “[w]ith respect to any referenced contract or class of referenced contracts, the Commission may make a determination that any swap or class of swaps satisfies, or does not satisfy, this economically equivalent swap definition.”

In the preamble, the CFTC explained that terms that are “unique to swaps” are immaterial.<sup>30</sup> Consequently, the following terms and conditions are not material when determining whether a swap is an economically equivalent swap: clearing arrangements, governing law, designating business day or holiday conventions; day count; calculation agent; dispute resolution mechanisms; choice of law; or representations and warranties.<sup>31</sup>

#### C. Good Faith Determination of Whether a Swap is an Economically Equivalent Swap

As noted above, the determination of whether a swap is economically equivalent to a referenced futures contract requires a “a facts and circumstances analysis.”<sup>32</sup> In the preamble, the CFTC expressly acknowledged that market participants, many of which have a long history of negotiating and documenting the contractual terms of OTC swap agreements, have the knowledge and experience necessary “to determine whether particular swaps share identical material terms with referenced contracts and would therefore qualify as ‘economically equivalent’ for purposes of Federal position limits.”<sup>33</sup>

The Commission effectively provided market participants with a safe harbor against enforcement action provided that they satisfy two conditions when determining whether a swap is an economically equivalent swap. A market participant must: “(i) perform[] the necessary

<sup>29</sup> Appendix A to this memorandum does not address the “delivery date” divergence issue because the CFTC’s discussion of delivery date divergence only appears in the context of so-called “physically delivered swaps.” See, e.g., 86 Fed. Reg. at 3291-94, 3296. To date, we have not received an example of a physically-delivered swap.

<sup>30</sup> *Id.* at 3291.

<sup>31</sup> *Id.*

<sup>32</sup> *Id.* at 3295.

<sup>33</sup> *Id.*

due diligence and [be] able to provide sufficient evidence, if requested, to support its reasonable, good faith determination that the swap is or is not an economically equivalent swap and (ii) come[] into compliance with the applicable Federal position limits within a commercially reasonable time, as determined by the Commission in consultation with the market participant, and if applicable, any relevant exchange.”<sup>34</sup> The CFTC believes that this approach should provide market participants with “a greater level of certainty” rather than first submitting “swaps to the Commission staff and wait[ing] for feedback before entering into swaps.”<sup>35</sup>

A market participant that follows the analysis set forth in this memorandum and analyzes swaps consistently with the approach set forth in Appendix A should satisfy the reasonable, good faith determination and sufficient evidence requirements of the first condition set by the Commission for protection against enforcement action if the CFTC later makes a different determination about the economic equivalence of a particular swap. It then will be up to the market participant to come into compliance with the CFTC’s determination within a commercially reasonable time.<sup>36</sup>

### III. Facts and Circumstances Analysis of Swaps Provided by Members of the FIA Working Group

Most commodity swaps are documented under an ISDA Master Agreement, a Schedule and a Confirmation. They also incorporate terms defined in the 2005 ISDA Commodity Definitions. Because the plain text of the Position Limits Rule and the CFTC’s guidance requires a comparison of the **contractual** terms of a swap and a particular referenced contract, for each sample confirmation provided to us by members of the Working Group, we examined the contractual terms of the swap and the particular referenced futures contract specified by the parties in the swap agreement.

#### A. Material Commodity Swap Contractual Terms

A typical commodity swap confirmation includes the contractual terms identified in **Appendix B** hereto. Based upon the CFTC’s guidance, the most important material contractual terms are the Effective date, Termination Date, Commodity, Settlement method, and Commodity Reference Price.<sup>37</sup>

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<sup>34</sup> *Id.* The CFTC further explained that “[a]s long as the market participant made the determination, prior to such Commission determination, using reasonable, good faith efforts, *the Commission would not take any enforcement action* for violating the Commission’s position limits regulations if the Commission’s determination subsequently differs from the determination of the market participant and the market participant comes into compliance with the applicable Federal position limits within a commercially reasonable time, as determined by the Commission in consultation with the market participant, and if applicable, any relevant exchange.” *Id.* (Emphasis added).

<sup>35</sup> *Id.* See also *id.* at 3415 (“The Commission anticipates that *this flexibility will benefit market integrity* by providing a greater level of certainty to market participants, in contrast to the alternative in which market participants would be required to first submit swaps to the Commission staff and wait for feedback or approval.” (Emphasis added)).

<sup>36</sup> *Id.* at footnote 437 (emphasis added).

<sup>37</sup> Capitalized terms have the meaning given them in the 2005 ISDA Commodity Definitions.

## **B. Material Referenced Futures Contract Contractual Terms**

A typical commodity futures contract includes the contractual specifications listed by the relevant DCM. See for example, the contract specifications of the NYMEX HENRY HUB NATURAL GAS FUTURES, the NYMEX NATURAL GAS (HENRY HUB) LAST-DAY FINANCIAL FUTURES and ICE Henry LD1 Fixed Price Future, attached hereto as Appendices C, D and E, respectively. Based upon the CFTC's guidance, the most important material contractual terms of a commodity futures contract are the Commodity, Listed Contracts, Settlement Method, Floating Price or Reference Price, and Termination of Trading.<sup>38</sup>

## **C. Analysis of Sample Confirmations**

For purposes of our analysis, the most relevant material contractual terms of a swap are the commodity reference price / commodity, the settlement type (physical or financial) and the term or duration of the contract. As noted above, a summary of our analysis is set forth in Appendix A.

### **1. Commodity / Commodity Reference Price and Settlement Type**

The commodity type material term is reasonably self-explanatory provided that the comparison between a swap and a particular reference contract takes into account any specified grade differentials. The Commodity Reference Price of most of the swap confirmations provided to us by the Working Group incorporated commodity reference prices defined in the 2005 ISDA Commodity Definitions. For example, in natural gas, certain swaps referenced "Natural Gas – Henry Hub – NYMEX," which is defined in Section 7.1, Sub-Annex A, of the 2005 ISDA Commodity Definitions.

Because the Commodity Reference Price in a swap points to a particular referenced futures contract, in order to determine whether the swap is an economically equivalent swap, the material contractual terms of the swap must be compared to the material contractual terms of the particular referenced futures contract. Comparing the material contractual terms of the swap with those of any other referenced futures contract would be inconsistent with the Commission's statement in the preamble that the Commodity Reference Price is one of the "material" provisions of a swap that drives its economic value and, therefore, is key to the analysis of whether a particular swap is an economically equivalent swap.<sup>39</sup>

Thus, if the Commodity Reference Price of a swap is "Natural Gas – Henry Hub – NYMEX", a market participant must compare the material contractual terms of the swap to the material contract specifications of the NYMEX HENRY HUB NATURAL GAS FUTURES contract, *i.e.*, the particular referenced futures contract that drives the economic value of the swap.<sup>40</sup> The material contractual terms of the NYMEX HENRY HUB NATURAL GAS FUTURES contract include commodity (natural gas), settlement method (deliverable) and term (monthly terminating on the 3<sup>rd</sup> last business day of the month prior to the contract month). If any of the material contract terms of the swap and the referenced futures contract are not identical, the swap is not an economically equivalent swap. In this example, the settlement types

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<sup>38</sup> Capitalized terms have the meaning given them in the relevant DCM futures contract specifications.

<sup>39</sup> 86 Fed. Reg. at 3291.

<sup>40</sup> See Appendix C.

of the swap (financial) and the referenced futures contract (physical) are not identical. Accordingly, the financially-settled swap is not economically equivalent to the physically-settled referenced futures contract. For the same reason, the financially-settled swaps in Appendix A that point in the Commodity Reference Price to a particular physically-settled referenced futures contract should not be characterized as economically equivalent swaps.

## 2. Term or Duration

DCMs list futures contracts with identified settlement months that expire at a specific point in time specified in the contract specifications. In order to be economically equivalent, a swap must have a term that is identical to the term of the referenced futures contract specified in the Commodity Reference Price. The only swaps that have a term that is the same as a referenced futures contract are so called-bullet swaps that settle based upon the final settlement price of a single futures contract. To the extent the term or duration of a swap has a term or duration that exceeds the term of a single futures contract, the term or duration of the swap is not identical to a referenced futures contract. Thus, even if all other material terms of a swap are identical to those of a referenced futures contract, if the durations of the swap and the referenced futures contract differ, they are not economically equivalent.

As shown on Appendix A, in addition to having different settlement types, most of the swaps provided to us by the Working Group have different durations than the particular referenced futures contract specified in the Commodity Reference price. For this reason, those swaps should not be characterized as economically equivalent swaps.

### D. Economically Equivalent Swap Example

Although not included among the swaps analyzed in Appendix A, if a financially-settled swap specified as its Commodity Reference Price the price of a financially-settled futures contract (*e.g.*, the ICE Futures U.S. Henry LD1 Fixed Price Future—see the contract specifications in **Appendix E**), the swap would be an economically equivalent swap provided all other material contractual terms are identical). In this regard, the Commission explained that “a cash-settled swap that either settles to the pricing of a corresponding cash-settled referenced contract, or incorporates by reference the terms of such referenced contract, would be deemed to be economically equivalent to the referenced contract.”<sup>41</sup> To illustrate, we have attached as **Appendix F** a hypothetical swap that uses as its Commodity Reference Price “NYMEX NATURAL GAS (HENRY HUB) LAST-DAY FINANCIAL FUTURES” with a term of March 29 – March 29, 2023. In this example, the commodity, Commodity Reference Price, settlement type and term of the swap and the referenced futures contract are identical. Hence, the swap would qualify as an economically equivalent swap.

### E. The Current or Future Existence of a Financially-Settled Referenced Futures Contract Should Not Convert a Swap that Specifies a Physically-Settled Referenced Futures Contract as its Commodity Reference Price into an Economically Equivalent Swap

In the preamble to the Position Limits Rule, the CFTC commented that “a cash-settled swap that initially did not qualify as ‘economically equivalent’ due to no corresponding cash-

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<sup>41</sup> Position Limits Rule 3291.

settled referenced contract (*i.e.*, no cash-settled look-alike futures contract) *could subsequently become an ‘economically equivalent swap’ if a cash-settled futures contract market were to develop.*<sup>42</sup> The CFTC also commented that “cash-settled swaps are subject to position limits only if there is a corresponding (*i.e.*, ‘economically equivalent’) cash-settled futures contract or option on a futures contract.”<sup>43</sup> For several reasons, we do not believe that the Commission intended by either of these comments to say that a swap that specifies in its Commodity Reference Price the price of a physically-settled referenced futures contract could be transformed into an economically equivalent swap simply because of the current existence or subsequent creation of a financially-settled look-a-like referenced futures contract.

First, the CFTC stated unequivocally that the Commodity Reference Price is a material contract term. Consequently, where the parties to a swap contract specify as the Commodity Reference Price a physically-settled referenced futures contract, the Commodity Reference Price is *not* identical to the financially-settled referenced futures contract and, thus, the swap is *not* economically equivalent to the financially-settled referenced futures contract. An alternative interpretation that a swap, which specifies as its Commodity Reference Price a physically-settled referenced futures contract, could be economically equivalent to a financially-settled look-a-like referenced futures contract would nullify Commodity Reference Price as a material term.

Second, the CFTC also identified settlement type as a material contract term. A swap that includes a Commodity Reference Price that is based upon the price of a physically-settled referenced futures contract is not an economically equivalent swap because the settlement type of the swap (financially-settled) is not identical to the settlement type (physical) of the particular physically-settled referenced futures contract specified in the swap. Third, such an interpretation would open the door to the type of netting of referenced contracts that CFTC sought to preclude through its intentionally narrow definition of economically equivalent swap. Fourth, as a matter of basic contract law, the current existence or subsequent creation of a financially-settled referenced futures contract cannot amend the Commodity Reference Price of a swap absent the consent of the parties.<sup>44</sup>

Finally, characterizing a swap as economically equivalent when it specifies a physically-settled futures contract as its Commodity Reference Price would substantively amend the definition of economically equivalent swap to be the same as the definition of referenced futures

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<sup>42</sup> *Id.* at 3291 (emphasis added).

<sup>43</sup> *Id.* at 3293 and n.424.

<sup>44</sup> The following example illustrates one reason why a swap that uses as its Commodity Reference Price a physically-settled referenced futures contract should not be interpreted as economically equivalent to a financially-settled look-alike referenced futures contract. Assume that a bullet swap names the NYMEX physically-settled natural gas futures contract, NG, as its Commodity Reference Price. See Appendix C. NG is a Core Reference Futures Contract. The settlement of the bullet swap is calculated based upon the closing price on the last trading day of the spot month. ICE lists a financially-settled natural gas futures contract, LD1, the specifications of which include NG as its Reference Price. See Appendix E. Assume that the NG contract on the last trading day for the spot month closes at \$6.00 per MMBtu. According to its specifications, the LD1 contract also would settle at \$6.00. Now assume that, due to some extraneous event, the underlying cash price for natural gas at Henry Hub is quoted by some market participants at prices between \$6.05 and \$6.10 / MMBtu. CME nevertheless allows the \$6.00 settlement of the NG contract to stand. ICE, however, acting pursuant to its recently amended Rule 4.34, revises the final settlement price of the LD1 contract to \$6.05 on the grounds that LD1’s Settlement Price was erroneous. Based upon the material contractual terms of the swap, the settlement of the swap will be calculated based upon the NG contract settlement of \$6.00. It is, therefore, the material specifications, terms and conditions of the NG contract, not the LD1 contract, that in the Commission’s words “drive the economic value of the swap.” *Id.* at 3291.

contract. It would focus solely on price linkage between the swap and the futures contract rather than on whether the material contract terms of the two contracts are the same. Furthermore, it would contradict the CFTC's considered determination to adopt a definition of economically equivalent swap that is narrower than the definition of referenced futures contract.<sup>45</sup>

Based upon the plain text of the definition of economically equivalent swap and the Commission's guidance in the preamble, in order for a financially-settled swap to have material contract terms that are identical to those of a referenced futures contract, the swap must specify as its Commodity Reference Price a particular financially-settled look-a-like referenced futures contract. Accordingly, the most logical and rational interpretation of the CFTC's comments about existing or as-yet-to-be-created financially-settled look-a-like referenced futures contracts is that if a swap uses the price of such a look-a-like referenced futures contract as its Commodity Reference Price, then the swap may be an economically equivalent swap (all other material terms being identical).

#### IV. Conclusion

We believe that the foregoing legal and "facts and circumstances" analysis satisfies the CFTC's requirement that market participants perform due diligence and make a reasonable, good faith determination concerning whether an OTC swap falls within the CFTC's intentionally narrow definition of economically equivalent swap. It also provides strong support for the determination that the swaps analyzed in Appendix A should not reasonably be characterized as economically equivalent swaps.

\* \* \* \* \*

This confidential memorandum is intended to serve as a reference for members of the FIA Position Limits Working Group as they analyze their swap portfolios in order to comply with federal position limits on economically equivalent swaps as of January 1, 2023. It is not a legal opinion or a guaranty of outcomes on any of the issues discussed above, but rather is an analysis of the legal authority applicable to the matters discussed herein. To the extent that any of the issues discussed in this memorandum are litigated, it is possible that a court could reach a different conclusion. To the extent that our analysis is dependent on factual matters, we have relied, without independent investigation, on information provided to us by the Working Group. This memorandum may not be quoted or distributed beyond FIA and members of the FIA Position Limits Working Group without our prior consent.

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<sup>45</sup> *Id.* at 3289. During our meeting on July 13, 2022, CFTC Staff asked the following question:

- If  $A = B$  (A is the physically-settled futures contract, and B is the cash-settled referenced contract); and
- $B = C$  (B is the cash-settled referenced contract, and C is a swap that is economically equivalent to B); then
- Why does  $C \neq A$  (C is a swap and A is the physically-settled futures contract)?

The reason why C does not equal A is because the methodology in the definition of referenced contract used to compare A and B (price linkage) is not the same as the methodology in the definition of economically equivalent swap used to compare C to either A or B (whether the material contract terms are identical).

## APPENDIX A – Economically Equivalent Swaps Analysis

Underlying Commodity	Term / Maturity / Other Specifications	Commodity Reference Price (CRP)	Settlement Type (Futures Contract / Swap)	Economically Equivalent?
Natural Gas	Jun 1–30, 2022	NATURAL GAS-HENRY HUB-NYMEX	Physical / Financial	No. The settlement type in the swap (financial) is not identical to the settlement type of the futures contract in the CRP (physical).
Natural Gas	Jan 1 – Dec 31, 2024	“Monthly Bidweek Spot Gas Prices (\$/MMBtu): Appalachia: Texas Eastern, M-2 receipts: Index” in the issue of Inside FERC that reports prices effective on that Pricing Date.	Physical / Financial	No. The term is not identical to a referenced futures contract. Also, an “outright price reporting agency index contract” is excluded from the definition of referenced contract.
Natural Gas	Nov 1, 2024 – Mar 31, 2025 European Collar	NATURAL GAS-HENRY HUB-NYMEX	Physical / Financial	No. Neither the term nor the collar structure is identical to a referenced futures contract. The settlement type in the swap (financial) is not identical to the settlement type of the futures contract in the CRP (physical).
Oil-WTI	Jan 1 - Dec 31, 2024	OIL-WTI-NYMEX	Physical / Financial	No. Neither the term nor the settlement type in the swap (financial) is identical to the futures contract in the CRP (physical).
Oil-WTI	Jan 1 – Dec 31, 2023 Three-Way Collar	OIL-WTI-NYMEX	Physical / Financial	No. Neither the term nor the three-way collar structure is identical to a referenced futures contract. The settlement type in the swap (financial) is not identical to the settlement type of the futures contract in the CRP (physical).



<b>Underlying Commodity</b>	<b>Term / Maturity / Other Specifications</b>	<b>Commodity Reference Price (CRP)</b>	<b>Settlement Type (Futures Contract / Swap)</b>	<b>Economically Equivalent?</b>
Oil	Feb 1 – Dec 31, 2022 Asian Collar or Swap	OIL-BRENT-IPE	Physical / Financial	No. Neither the term nor the settlement type in the swap (financial) is identical to the futures contract in the CRP (physical).
OIL-WTI Oil - Brent	Jun 1-30, 2022	OIL-WTI-ICE OIL-BRENT-IPE	Physical / Financial	No. The CRP is not identical to the price of a single referenced futures contract.
Oil-WTI	Jan 1, 2019 – Dec 31, 2022	OIL-WTI-ICE	Physical / Financial	No. The term is not identical to the referenced futures contract.
Heating Oil Gasoline Oil - Brent	Jan 1-31, 2023	OIL-BRENT-IPE HEATING OIL-NEW YORK-NYMEX GASOLINE-RBOB-NEW YORK-NYMEX	Physical / Financial	No. The CRP is not identical to the price of a single referenced futures contract.
Heating Oil	Mar 30, 2022 – Mar 30, 2022 Penultimate bullet swap	HEATING OIL-NEW YORK-NYMEX	Physical / Financial	No. The settlement type in the swap (financial) is not identical to the settlement type of the futures contract in the CRP (physical).
Gasoline	Mar 30, 2022 – Mar 30, 2022 Penultimate bullet swap	GASOLINE-RBOB-NEW YORK-NYMEX	Physical / Financial	No. The settlement type in the swap (financial) is not identical to the settlement type of the futures contract in the CRP (physical).
Gold	Aug 1-31, 2022	The official COMEX settlement price of the August 2022 contract month for Gold.	Physical / Financial	No. The settlement type in the swap (financial) is not identical to the settlement type of the futures contract in the CRP (physical).

<b>Underlying Commodity</b>	<b>Term / Maturity / Other Specifications</b>	<b>Commodity Reference Price (CRP)</b>	<b>Settlement Type (Futures Contract / Swap)</b>	<b>Economically Equivalent?</b>
Gold	July 2021 – May 2022	Gold – COMEX	Physical / Financial	No. Neither the term nor the settlement type in the swap (financial) is identical to the futures contract in the CRP (physical).
Copper	May 1 – Oct 31, 2022	COPPER-COMEX	Physical / Financial	No. Neither the term nor the settlement type in the swap (financial) is identical to the futures contract in the CRP (physical).
Copper	Apr 2022 – Mar 2023	Copper – COMEX	Physical / Financial	No. Neither the term nor the settlement type in the swap (financial) is identical to the futures contract in the CRP (physical).
Lean Hogs	Jun 1–30, 2022	LEAN HOGS-CME	Physical / Financial	No. The settlement type in the swap (financial) is not identical to the settlement type of the futures contract in the CRP (physical).
Livestock	Jun 1-30, 2022	LIVE CATTLE-CME	Physical / Financial	No. The settlement type in the swap (financial) is not identical to the settlement type of the futures contract in the CRP (physical).
Coffee	Jul 1-31, 2022	COFFEE ARABICA-NYBOT	Physical / Financial	No. The settlement type in the swap (financial) is not identical to the settlement type of the futures contract in the CRP (physical).
Sugar	Dec 2022 – Sept 2023	Sugar # 11 (World) ICE Futures U.S.	Physical / Financial	No. Neither the term nor the settlement type in the swap (financial) is identical to the futures contract in the CRP (physical).

<b>Underlying Commodity</b>	<b>Term / Maturity / Other Specifications</b>	<b>Commodity Reference Price (CRP)</b>	<b>Settlement Type (Futures Contract / Swap)</b>	<b>Economically Equivalent?</b>
Cotton	Jan 2022 – Apr 2022 (option)	Cotton no. 2 – ICE Futures U.S.	Physical / Financial	No. Neither the term nor the settlement type in the swap (financial) is identical to the futures contract in the CRP (physical).
Corn	Sept 2021 – Nov 2022 (option)	Corn – CBOT	Physical / Financial	No. Neither the term nor the settlement type in the swap (financial) is identical to the futures contract in the CRP (physical).
Wheat	April 2022 – June 2022	Wheat - CBOT	Physical / Financial	No. Neither the term nor the settlement type in the swap (financial) is identical to the futures contract in the CRP (physical).
Commodity Index	Apr 2022 – Jul 2022	[Redacted] Commodity Index	Physical / Financial	No. The [Redacted] index references the BCOM index, among other components, and therefore references price of more than 1 different commodity. Accordingly, the swap meets the definition of a commodity index contract excluded from position limits.
Commodity Index	Apr 2022 – Apr 2023	Bloomberg Commodity Index Total Return	Physical / Financial	No. The BCOM index references the price of more than 1 different commodity, so the swap meets the definition of a commodity index contract excluded from position limits.

**Additional Provisions for a  
Confirmation of a Commodity Swap / Basis Swap**

[See Exhibit I for the introduction, standard paragraphs and closing for the letter agreement or facsimile.]

1. The terms of the particular Transaction to which this Confirmation relates are as follows:

**General Terms:**

Trade Date: [ ]  
 Effective Date: [ ]  
 Termination Date: [ ]  
 Commodity / Commodities: [A/B]<sup>1</sup>  
 [Total Notional Quantity: [Amount in numerals][Units of Commodity]]  
 [Notional Quantity per Calculation Period: [Amount in numerals][Units of Commodity]]<sup>2</sup>  
 [Calculation Period(s): [ ]]  
 [Settlement Period(s)]:<sup>3</sup> [ ]  
 [Applicable Days: [ ]]  
 [Duration: [Hourly][Half-hourly ]]  
 [Start Time / End Time: [\_\_\_\_][Time zone]]  
 [\_\_\_\_][Time zone]] ]  
 [Settlement][Payment] Date(s): [Specify details][, subject to adjustment in accordance with the [Following/Modified Following/Nearest/Preceding] Business Day Convention]<sup>4</sup>

[Common Pricing[Applicable]]<sup>5</sup>  
 Business Day: [city]

**Fixed Amount Details:**

Fixed Price Payer: Party [A/B]  
 Fixed [Amount/Price]: [currency][amount in numerals][per Units of Commodity]

**Floating Amount Details [I]:<sup>6</sup>**

Floating Price Payer: Party [B/A]  
 [Applicable spread: [+/-][ %][[currency][amount in numerals]]]<sup>7</sup>  
 [Floating Price: [ ]]  
 Commodity Reference Price: [ ]<sup>8</sup>  
 [Unit: [ ]]

<sup>1</sup> The parties may specify more than one Commodity for a Transaction with more than one Floating Price Payer, such as a commodity basis swap transaction.

<sup>2</sup> The parties may specify a different Notional Quantity per Calculation Period for each party. In addition, the parties may specify a different Notional Quantity (or a formula for determining that Notional Quantity) for each Calculation Period.

<sup>3</sup> Parties may specify the Settlement Period(s) and each of the three following provisions for a Transaction in conjunction with any Calculation Period relating to a Commodity Reference Price for Electricity.

<sup>4</sup> If it is contemplated that the Payment Dates for (i) the Fixed Price Payer and the Floating Price Payer or (ii) the Floating Price Payer and the Floating Price Payer, as applicable, will not match, include such dates for the parties in (i) the Fixed Amount Details and the Floating Amount Details sections or in (ii) each of the Floating Amount Details sections of the Confirmation rather than at this point in the Confirmation.

<sup>5</sup> Common Pricing may be relevant for a Transaction that references more than one Commodity Reference Price. If Common Pricing is not specified as Applicable, it will be deemed not to apply.

<sup>6</sup> Indicate "I" if more than one Floating Price Payer and include below the Floating Amount Details for the second Floating Price Payer.

<sup>7</sup> Parties may choose to specify the applicable spread, which may be expressed as a percentage, in currency units or as otherwise agreed by the parties.

<sup>8</sup> The parties may either: (i) specify one of the Commodity Reference Prices defined in the Commodity Definitions; or (ii) create a Commodity Reference Price by specifying a Commodity, a Unit, a Price Source and a Currency under the Commodity Reference Price Framework.

Price Source/Reference	[ ]
Dealers:	
Currency:	[ ] <sup>9</sup>
Specified Price:	[Specify whether the price will be the bid price, the ask, price, the average of the high and low prices, the morning fixing, etc.; if appropriate, indicate the time as of which the price is to be determined]
[Delivery Date:]	[Specify whether the price will be based on a certain delivery date or month (e.g., the spot market, the First Nearby Month, the Second Nearby Month, etc. or some other methodology)]
Pricing Date(s):	[Specify details][, subject to adjustment in accordance with the [Following/Modified Following/Nearest/Preceding] Commodity Business Day Convention] <sup>10</sup>
[Method of Averaging:	[ ] <sup>11</sup>
[Currency Conversion Provision:	[ ] <sup>12</sup>
<b>[Market Disruption:]</b>	
[Market Disruption Event(s):	[Not Applicable][ ] <sup>13</sup>
[Additional Market	[ ] <sup>14</sup>
Disruption Event(s):	
[Disruption Fallback(s):	[ ] <sup>15</sup>
[Fallback Reference Price:	[ ] <sup>16</sup>
[Maximum Days of	[ ] <sup>17</sup>
Disruption:	
<b>[Floating Amount Details II:</b>	[ ] <sup>18</sup>

<sup>9</sup> Delete if a Commodity Reference Price (other than Commodity Reference Dealers), which is already defined in the Commodity Definitions, is specified above.

<sup>10</sup> The parties must specify the date or dates, or the means for determining the date or dates, on which a price will be obtained (including any applicable Commodity Business Day Convention) for purposes of calculating the Floating Amount, e.g., each Commodity Business Day during the Calculation Period or the last three Commodity Business Days in each Calculation Period. If Common Pricing has been specified as applicable, then a Pricing Date must be a day on which all referenced Commodity Reference Prices are scheduled to be published or announced, as determined on the Trade Date of the Transaction as of the time of execution of the Transaction.

<sup>11</sup> The parties may specify a Method of Averaging where more than one Pricing Date is specified above as being applicable to a Calculation Period or a Payment Date. If not specified, unweighted arithmetic mean shall apply in accordance with Section 6.2 of the Commodity Definitions.

<sup>12</sup> Include a Currency Conversion Provision for a Transaction with a Commodity Reference Price that is denominated in a currency other than in the agreed currency of payment.

<sup>13</sup> Parties wishing to agree to Market Disruption Events may do so or may rely on the standard fallback approach of Section 7.4(d)(i) of the Commodity Definitions. Parties may also indicate the inapplicability of Market Disruption Events.

<sup>14</sup> Parties relying on the standard fallback Market Disruption Events of Section 7.4(d)(i) of the Commodity Definitions may also wish to agree to Additional Market Disruption Events.

<sup>15</sup> Parties wishing to agree to Disruption Fallbacks may do so or may rely on the standard fallback approach of Section 7.5(d)(i) of the Commodity Definitions.

<sup>16</sup> The parties should specify an alternate Commodity Reference Price if they are relying on the Disruption Fallbacks set forth in Section 7.5(d)(i) of the Commodity Definitions or if they have otherwise specified "Fallback Reference Price" as applicable.

<sup>17</sup> Parties selecting Disruption Fallbacks should specify the Maximum Days of Disruption, unless they wish 5 Commodity Business Days to apply pursuant to Section 7.6(a) of the Commodity Definitions. Parties relying on Section 7.5(d)(i) of the Commodity Definitions will be subject to 2 Commodity Business Days, as set forth in that Section, unless they choose to affirmatively overcome that provision.

<sup>18</sup> Parties to a commodity basis swap transaction may state full Floating Amount Details here for the second Floating Price Payer.

APPENDIX C

**NYMEX HENRY HUB NATURAL GAS FUTURES - CONTRACT SPECS<sup>1</sup>**

<b>CONTRACT UNIT</b>	10,000 MMBtu
<b>PRICE QUOTATION</b>	U.S. dollars and cents per MMBtu
<b>TRADING HOURS</b>	<p><b>CME Globex:</b>            Sunday - Friday 6:00 p.m. - 5:00 p.m. (5:00 p.m. - 4:00 p.m. /CT) with a 60-minute break each day beginning at 5:00 p.m. (4:00 p.m. CT)</p> <p>TAS: Sunday - Friday 6:00 p.m. - 2:30 p.m. (5:00 p.m. - 1:30 p.m. CT)</p> <p><b>CME ClearPort:</b>            Sunday 5:00 p.m. - Friday 4:00 p.m. CT with no reporting Monday - Thursday from 4:00 p.m. – 5:00 p.m. CT</p>
<b>MINIMUM PRICE FLUCTUATION</b>	<p><b>CME Globex:</b>            Intercommodity spreads: 0.00025 per MMBtu = \$2.50</p> <p>TAS: Zero or +/- 10 ticks in the minimum tick increment of the outright</p> <p><b>Outright:</b>            0.001 per MMBtu = \$10.00</p>
<b>PRODUCT CODE</b>	<p><b>CME Globex:</b> NG      <b>CME ClearPort:</b> NG      <b>Clearing:</b> NG      <b>TAS:</b> NGT</p>
<b>LISTED CONTRACTS</b>	Monthly contracts listed for the current year and the next 12 calendar years. List monthly contracts for a new calendar year following the termination of trading in the December contract of the current year.
<b>SETTLEMENT METHOD</b>	Deliverable

<sup>1</sup> Source: <https://www.cmegroup.com/markets/energy/natural-gas/natural-gas.contractSpecs.html>

**TERMINATION OF TRADING**

Trading terminates on the 3rd last business day of the month prior to the contract month.

**TAM OR TAS RULES**

Trading at Settlement (TAS) is subject to the requirements of Rule 524.A. TAS trades off a “Base Price” of zero (equal to the daily settlement price) to create a differential versus the daily settlement price in the underlying futures contract month. The TAS clearing price equals the daily settlement price of the underlying futures contract month plus or minus the TAS transaction price.

[TAS Table](#)

**SETTLEMENT PROCEDURES**

[Natural Gas Futures Settlement Procedures](#)

**POSITION LIMITS**

[NYMEX Position Limits](#)

**EXCHANGE RULEBOOK**

[NYMEX 220](#)

**BLOCK MINIMUM**

[Block Minimum Thresholds](#)

**PRICE LIMIT OR CIRCUIT**

[Price Limits](#)

**VENDOR CODES**

[Quote Vendor Symbols Listing](#)

**GRADE AND QUALITY**

Natural Gas meeting the specifications set forth in the FERC-approved tariff of Sabine Pipe Line Company as then in effect at the time of delivery shall be deliverable in satisfaction of futures contract delivery obligations.

**APPENDIX D**

**NYMEX NATURAL GAS (HENRY HUB) LAST-DAY FINANCIAL FUTURES – CONTRACT SPECS<sup>1</sup>**

<b>CONTRACT UNIT</b>	10,000 MMBtu				
<b>PRICE QUOTATION</b>	U.S. dollars and cents per MMBtu				
<b>TRADING HOURS</b>	<p><b>CME Globex:</b>                  Sunday - Friday 6:00 p.m. - 5:00 p.m. (5:00 p.m. - 4:00 p.m. CT) with a 60-minute break each day beginning at 5:00 p.m. (4:00 p.m. CT)</p> <p>TAS: Sunday - Friday 6:00 p.m. - 2:30 p.m. (5:00 p.m. - 1:30 p.m. CT)</p> <p><b>CME ClearPort:</b>                  Sunday 5:00 p.m. - Friday 4:00 p.m. CT with no reporting Monday - Thursday from 4:00 p.m. – 5:00 p.m. CT</p>				
<b>MINIMUM PRICE FLUCTUATION</b>	<p><b>CME Globex:</b>                  Inter-commodity spreads: 0.00025 per MMBtu = \$2.50</p> <p>TAS: Zero or +/- 10 ticks in the minimum tick increment of the outright</p> <p><b>Outright:</b>                  0.001 per MMBtu = \$10.00</p>				
<b>PRODUCT CODE</b>	<b>CME Globex: HH</b>	<b>CME ClearPort: HH</b>	<b>Clearing: HH</b>	<b>TAS: HHT</b>	<b>TAM: HHE</b>
<b>LISTED CONTRACTS</b>	Monthly contracts listed for the current year and the next 12 calendar years. List monthly contracts for a new calendar year following the termination of trading in the December contract of the current year.				
<b>SETTLEMENT METHOD</b>	Financially Settled				

<sup>1</sup> Source: <https://www.cmegroup.com/markets/energy/natural-gas/natural-gas-last-day.contractSpecs.html>



**FLOATING PRICE**

The Floating Price for each contract month will be equal to the NYMEX (Henry Hub) Natural Gas Futures contract final settlement price for the corresponding contract month on the last trading day for that contract month.

**TERMINATION OF TRADING**

Trading terminates on the third last business day of the month prior to the contract month.

**TAM OR TAS RULES**

Trading at Settlement (TAS) is subject to the requirements of Rule 524.A. TAS trades off a “Base Price” of zero (equal to the daily settlement price) to create a differential versus the daily settlement price in the underlying futures contract month. The TAS clearing price equals the daily settlement price of the underlying futures contract month plus or minus the TAS transaction price.

[TAS Table](#)

**SETTLEMENT PROCEDURES**

Delivery under the NYMEX Henry Hub contract shall be by cash settlement. Final settlement, following termination of trading for a contract month, will be based on the Floating Price. The final settlement price will be the Floating Price calculated for each contract month

[Natural Gas \(Henry Hub\) Last-day Financial Futures Settlement Procedures](#)

**POSITION LIMITS**

[NYMEX Position Limits](#)

**EXCHANGE RULEBOOK**

[NYMEX 823](#)

**BLOCK MINIMUM**

[Block Minimum Thresholds](#)

**PRICE LIMIT OR CIRCUIT**

[Price Limits](#)

**VENDOR CODES**

[Quote Vendor Symbols Listing](#)



## Henry LD1 Fixed Price Future<sup>1</sup>

### Contract Specifications

Description	A monthly cash settled Exchange Futures Contract based upon the monthly price published by NYMEX for the location specified in Reference Price A.
Contract Symbol	H
Settlement Method	Cash settlement
Contract Size	2500 MMBtus
Currency	USD
Minimum Price Fluctuation	The price quotation convention shall be One tenth of a cent (\$0.001) per MMBtu; minimum price fluctuation may vary by trade type. Please see Table in Resolution 1 to this Chapter 18.
Listing Cycle	Up to 156 consecutive monthly Contract Periods
Last Trading Day	Three Business Days prior to the first calendar day of the Contract Period
Final Settlement	Reference Price A
REFERENCE PRICE A	NATURAL GAS-NYMEX
a) Ref Price A - Description	“NATURAL GAS-NYMEX” means that the price for a Pricing Date will be that day’s Specified Price per MMBTU of natural gas on the NYMEX of the Henry Hub Natural Gas Futures Contract for the Delivery Date, stated in U.S. Dollars, as made public by the NYMEX on that Pricing Date.

<sup>1</sup> Source: <https://www.theice.com/products/6590258/Henry-LD1-Fixed-Price-Future>

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b) Ref Price A - Pricing Date	Last scheduled trading day of the NYMEX Henry Hub Natural Gas Futures Contract for the Delivery Date
c) Ref Price A - Specified Price	Settlement price
d) Ref Price A - Pricing calendar	NYMEX
e) Ref Price A - Delivery Date	Contract Period
Final Payment Date	The first Clearing Organization business day following the Last Trading Day
Markers	TAS (Trade at Settlement)

APPENDIX F

**Example of Economically Equivalent Swap**

1. The terms of the particular Transaction to which this Confirmation relates are as follows:

**General Terms:**

Trade Date:	June 14, 2022
Effective Date:	March 29, 2023
Termination Date:	March 29, 2023
Commodity:	Natural Gas
Total Notional Quantity:	120,000 MMBtu
Notional Quantity per Calculation Period:	120,000 MMBtu
Calculation Period(s):	From and including March 29, 2023 to and including March 29, 2023
Business Day:	New York, New York

**Fixed Amount Details:**

Fixed Price Payer:	Party B
Fixed Price:	\$X.XX/MMBtu

**Floating Amount Details:**

Floating Price Payer:	Party A
Floating Price:	As per Commodity Reference Price
Commodity Reference Price:	NYMEX NATURAL GAS (HENRY HUB) LAST-DAY FINANCIAL FUTURES
Pricing Date(s):	From and including March 29, 2023 to and including March 29, 2023, subject to Market Disruption Events

**[Market Disruption:]**

[Market Disruption Event(s):	[Not Applicable][ ]]
[Additional Market Disruption Event(s):	[ ]]
[Disruption Fallback(s):	[ ]]
[Fallback Reference Price:	[ ]]
[Maximum Days of Disruption:	[ ]]